MATAV CABLE SYSTEMS MEDIA LTD
Form 20-F
June 30, 2003

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D)
OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the fiscal year ended December 31, 2002
Commission file number: 0-28556**

MATAV CABLE SYSTEMS MEDIA LTD.

(Exact name of Registrant as specified in its charter)

Israel
(Jurisdiction of incorporation or organization)

**42 Pinkas Street
North Industrial Park
P.O. Box 13600
Netanya 42134
Israel
(Address of principal executive offices)**

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Title of Each Class

American Depositary Shares
Ordinary Shares*

* Not for trading, but only in connection with the registration of American Depositary Shares representing such ordinary shares, pursuant to the requirements of the Securities and Exchange Commission.

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock as of the close of the period covered by the annual report:

Ordinary Shares of NIS 1.00 each **30,203,917**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days:

Yes x No o

Indicate by check mark which financial statement item the Registrant has elected to follow:

Item 17 o Item 18 x

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INTRODUCTION

As used herein, references to we, our, us, Matav or the Company are references to Matav-Cable Systems Media Ltd. and to its significant subsidiaries, including, Matav Investments Ltd., Cable Systems Media Haifa-Hadera Ltd., Nonstop Internet (1999) Ltd., Matav Assets Ltd., Matav Infrastructure Ltd. and Matav Infrastructure 2001,L.P., all of which are wholly owned subsidiaries, and Nonstop Ventures, Ltd.

In this document, references to $, US$, US dollars and dollars are to United States dollars and references to NIS and shekels are Israeli Shekels. This annual report contains translations of NIS amounts into US dollars at specified rates solely for the convenience of the reader. No representation is made that the amounts referred to in this annual report as convenience translations could have been or could be converted from NIS into US dollars at these rates, at any particular rate or at all. The translations of NIS amounts into US dollars appearing throughout this annual report have been made at the representative exchange rate on December 31, 2002 of NIS 4.737= US$1.00 as published by the Bank of Israel, unless otherwise specified. See Item 3A. Key Information Selected Financial Data Exchange Rate Data.

We maintain our financial books and records in shekels and present our financial statements in conformity with generally accepted accounting principles in Israel, or Israeli GAAP. As applicable to our financial statements, Israeli GAAP and U.S. GAAP vary in certain respects, as described in Note 20 to the financial statements. We present our historical statements in shekels that have been adjusted to reflect changes in purchasing power due to changes in the Israeli consumer price index. Unless otherwise specified in this annual report, all financial data relating to us are presented in shekels adjusted to December 31, 2002 purchasing power (adjusted NIS). See Item 5A. Operating and Financial Review and Prospects Operating Results Impact of Inflation and Exchange Rate Fluctuations and Note 15 to the financial statements.

FORWARD-LOOKING STATEMENTS

This annual report includes forward-looking statements within the meaning of Section 27A of the US Securities Act of 1933, as amended, Section 21E of the US Securities Exchange Act of 1934, as amended, and the safe harbor provisions of the US Private Securities Litigation Reform Act of 1995. We have based these forward-looking statements on our current expectations and projections about future events. These forward-looking statements are subject to risks, uncertainties and assumptions about us.

Words such as believe, anticipate, expect, intend, seek, will, plan, could, may, project, goal, target and similar identify forward-looking statements but are not the only way we identify these statements. All statements other than statements of historical fact included in this annual report, including the statements in the sections of this annual report entitled Item 3D. Key Information Risk Factors, Item 4. Information on the Company and Item 5. Operating and Financial Review and Prospects and located elsewhere in the annual report regarding our future performance, plans to increase revenues or margins or preserve or expand market share in existing or new markets, reduce expenses and any statements regarding other future events or our future prospects, are forward-looking statements.

We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including all the risks discussed in Item 3D. Key Information Risk Factors, Item 4. Information on the Company and Item 5. Operating and Financial Review and Prospects . In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this annual report might not occur.

PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

3A. SELECTED FINANCIAL DATA

The following table sets forth our selected consolidated financial data as at and for each of the years in the five-year period ended December 31, 2002. The selected consolidated financial data for the years ended December 31, 1998, 1999, 2000, 2001 and 2002 are based on consolidated financial statements that have been prepared in accordance with Israeli generally accepted accounting principles, or GAAP. As applied to our consolidated financial statements, Israeli GAAP and U.S. GAAP vary in certain respects, as described in Note 20 to the consolidated financial statements.

We were incorporated on June 28 1987. The selected consolidated financial data set forth below should be read in conjunction with Item 5. Operating and Financial Review and Prospects , and the financial statements and notes thereto included elsewhere in this report on Form 20-F. The financial data for the year ended as at December 31, 2002 have been translated into US dollars using the representative rate of exchange of the US dollar to the New Israeli Shekel, as published by the Bank of Israel, at December 31, 2002 (NIS4.737 = US$1.00). The translation is solely for convenience and should not be construed as a representation that Israeli currency amounts actually represent, or could be converted into US dollars.

	1998	1999	2000	2001	2002	2002
	NIS (in thousands) *	NIS (in thousands) *	NIS (in thousands) *	NIS (in thousands) *	NIS (in thousands) *	$ (in thousands)*
Revenues	450,217	490,743	483,791	478,362	505,009	106,609
Operating income (loss)	172,350	117,239	(62,796)	(132,333)	(100,567)	(21,230)
Financial expenses, net	24,828	9,431	34,984	53,083	(49,008)	(10,346)
Other income (expenses) net	(849)	448,672	1,026	3,111	283,859	59,924
Income (loss) before taxes on income	146,673	556,480	(96,754)	(182,305)	134,284	28,348
Equity in earnings (losses) of affiliated companies, net	(22,243)	(154,159)	(131,024)	(80,329)	11,119	2,347
Net income (loss), under Israeli GAAP	71,841	340,479	(227,952)	(262,192)	34,471	7,277
Net income (loss) per ordinary share, under Israeli GAAP	2.64	11.38	(7.88)	(9.09)	1.19	0.25
Net income (loss) per ADS, under Israeli GAAP	5.27	22.78	(15.77)	(18.18)	2.39	0.50
Weighted average number of shares outstanding in thousands, basic, under Israeli GAAP	27,232	29,899	28,914	28,834	28,860	28,860
ADS shares outstanding in thousands, basic - under Israeli GAAP	13,616	14,950	14,457	14,417	14,430	14,430
Net income (loss), under US GAAP		218,319	(223,616)	(219,761)	36,134	7,628
Net income (loss) per ordinary share, under US GAAP		8.01	(7.81)	(7.50)	1.25	0.26
Net income (loss) per ADS, under US GAAP		16.03	(15.63)	(15.00)	2.50	0.53
Weighted average number of shares outstanding in thousands, basic, under US GAAP		17,243	28,604	29,286	28,860	28,860
ADS shares outstanding in thousands, basic, under US GAAP		13,622	14,302	14,643	14,430	14,430
Capital expenditures	69,157	135,286	400,149	270,058	115,564	24,396
Balance Sheet Data:						
Fixed assets, net	605,316	645,401	929,878	1,058,035	1,010,961	213,418
Total assets, net	888,643	1,164,775	1,185,409	1,206,479	1,154,276	243,672
Short-term credit (including current maturities of bank loans and debentures)	178,375	50,929	254,455	572,152	558,325	117,865
Long-term bank loans	3,409	1,747	237,783	189,731	144,801	30,568
Debentures	203,004	174,113	145,217	135,002	101,363	21,399
	419,443	546,362	374,760	114,430	149,882	31,641

Shareholders equity under Israeli GAAP						
Shareholders equity under US GAAP	0	416	305,593	104,512	141,694	29,912
EBITDA	260,522	207,182	45,359	261	57,820	12,206

* The data set forth in the table above is expressed in NIS or US dollars, as applicable, except for data forth in the table regarding numbers of shares and ADSs, as applicable.

Exchange Rate Data

The following table sets forth, for the years indicated, exchange rates between the shekel and the US dollar, expressed as shekels per US dollar and based upon the daily representative rate of exchange on the last day of each year as published by the Bank of Israel.

	1998	**1999**	**2000**	**2001**	**2002**	**2003(2)**
Average(1)	3.76	4.14	4.077	4.214	4.736	4.641
High	4.37	4.29	4.198	4.416	4.994	4.924
Low	3.54	4.01	3.967	4.041	4.437	4.373
End of period	4.16	4.15	4.041	4.416	4.737	4.373

(1) Calculated based on the average of the exchange rates on the last day of each month during the relevant period.
(2) Through May 31, 2003.

	December 2002	**January 2003**	**February 2003**	**March 2003**	**April 2003**	**May 2003**
High	4.791	4.898	4.924	4.858	4.671	4.577
Low	4.632	4.737	4.810	4.687	4.521	4.373

At May 31, 2003, the representative rate of exchange was NIS 4.373 per US dollar, as published by the Bank of Israel.

Changes in the exchange rate between the shekel and the US dollar could affect our financial results.

Payment of Dividends to Shareholders

Our board of directors decided, on January 14, 1998, to distribute an interim cash dividend to our shareholders who held shares on February 15, 1998, in the nominal amount of NIS 2.5828 (approximately US$0.72) per ordinary share, for a total nominal amount of NIS 70 million, paid to the shareholders on March 2, 1998. Distribution of this dividend was approved as a final dividend for the year 1997 at our annual general meeting of shareholders held on November 18, 1998.

Our board of directors decided, on October 29, 1998, to distribute an interim cash dividend to our shareholders who held shares on November 18, 1998, in the nominal amount of NIS 2.9377 (approximately US$0.62) per ordinary share, for a total nominal amount of NIS 80 million, paid to the shareholders on December 3, 1998. Distribution of this dividend was approved as a final dividend for the years 1994, 1995 and 1996 at our annual general meeting of shareholders held on November 18, 1998.

Our board of directors decided, on December 27, 1999, to distribute an interim cash dividend to our shareholders who held shares on January 11, 2000, in the nominal amount of NIS 7.576 (approximately US$1.82) per ordinary share, for a total nominal amount of NIS 208.3 million paid to the shareholders on January 26, 2000. Distribution of this dividend was approved as a final dividend for the year 1999 at our annual general meeting of shareholders held on December 31, 2000. No dividends were declared in 2001 and 2002.

3B. CAPITALIZATION AND INDEBTEDNESS.

Not applicable.

3C. Reasons for the Offer and Use of Proceeds.

Not applicable.

3D. Risk Factors

In order to operate our business, we must have valid Licenses.

We conduct our operations pursuant to: two general non exclusive Cable Broadcast Licenses granted by the Council of Cable and Satellite Broadcasting on April 30, 2002; a general non-exclusive Telecommunications Infrastructure License granted by the Minister of Communications, on March 27, 2002; and a special Broadcasting HeadEnd License granted by the Minister of Communications on May 2, 2002.

The Cable Broadcast Licenses and the Telecommunications Infrastructure License are effective for a period of fifteen years and can be extended by additional ten-year periods if the Council (in respect of the Cable Broadcast Licenses), or the Minister (in respect of the Telecommunications Infrastructure License) determine that we have:

- complied with the terms and conditions of our Licenses and the applicable law and regulations;
- complied with the instructions of the Council and the Minister;
- continuously acted in a manner to improve our broadcasts, the technology of the broadcasts and the scope, availability and quality of our telecommunications services and our network technology;
- the ability to continue to provide the broadcasts and to invest in improvements of the broadcasts in the future, and the ability to continue to provide the telecommunications services and make necessary investments in order to update our technology and the scope, availability and quality of our telecommunications services; and
- continued to comply with the conditions upon which our Licenses have been granted.

Our Broadcasting HeadEnd License is valid for so long as our Cable Broadcast Licenses remain in force, but in any event no later than May 30, 2017, although we may apply for an extension of the Broadcasting HeadEnd License beyond this date.

In order to ensure compliance with our obligations pursuant to our Cable Broadcast and Telecommunications Infrastructure Licenses, applicable law and regulatory bodies, we have provided a bank guarantee in the amount of $10 million to the Minister of Communications (in respect of our Telecommunications Infrastructure License), and a bank guarantee in the amount of NIS 9 million to the Council (in respect of our Cable Broadcast Licenses). Each of the Minister and the Council has the authority to exercise the guarantees in the event that the Licensee does not fulfill its obligations, and to cover any damage, loss or cost that the Council, the Minister or the government may incur as a result of any breach of our obligations under the Licenses, and to ensure any payments by the Licensee, including royalty payments and payments of fines imposed by the Council or the Minister. The exercise of the guarantee does not derogate from the authority of the Council or the Minister to cancel the Licenses, to amend the terms and conditions of the Licenses or to impose other sanctions including fines for certain stipulated breaches or actions.

The Council or the Minister have the authority to amend the terms of our Licenses at any time, and, in relation to the Cable Broadcast Licenses, the Council must take into account any prejudice to the Licensee. Further, the Licenses may be cancelled for material breach of its provisions, or non-compliance with legal requirements, or non-remedy of a non-material breach. The Telecommunications Infrastructure License can further be cancelled by the Minister for non-supply of services, non-fulfillment of the conditions of receipt of the Licenses, breach of the restrictions upon the means of control of the Licensee entities, breach of cross ownership restrictions or breach of obligations to provide information to the Minister. We are also required to meet certain requirements pursuant to the Telecommunications Infrastructure License regarding the laying down of infrastructure.

Although we believe that we are currently in compliance with all material requirements of our Licenses, the interpretation and application of the standards used to measure these requirements may not be certain, and disagreements may arise in the future between us and the Minister of Communications or the Council.

We are subject to special regulatory restrictions applicable to monopolies, which limit our ability to control the conduct of our business.

On November 8,1999, the Controller of Restrictive Business Practices declared that we, and all the other cable television operators in Israel, constitute a monopoly in the provision of multi-channel cable television services in our then respective franchise areas (which are the same areas in which we operate pursuant to our current Licenses). On December 28, 1999, we filed an appeal of this declaration in the Restrictive Business Practices Court, which has not yet been decided. Until the appeal is finally resolved, and if the Controller of Restrictive Business Practices declaration is not dismissed, we are subject to the supervision of the Restrictive Business Practices Authority, in addition to the existing supervision of the Minister of Communications and the Council, including in the areas of pricing, quality of broadcasting services, agreements with our subscribers, agreements with content providers and the use of our cable television network. There can be no assurance that the declaration of the Controller of Restrictive Business Practices will be dismissed.

In February 2003, the other Israeli cable television operators and us agreed on a final version of an agreement, which sets forth the structure and conditions of a merger between us and the other Israeli cable television operators. This merger agreement, upon its signing, will be added to and broaden the terms of the previous arrangement between the parties executed on December 31, 2001 (further to previous arrangements between the parties that were cancelled and replaced). In the event that a merger with the other cable television operators in Israel is completed, the merged entities shall be subject to the supervision of the Controller of Restrictive Business Practices, and in addition, may be also subject to the above-mentioned restrictions as a monopoly.

The telecommunications industry in Israel is highly regulated which limits our flexibility to manage our business.

Our business is subject to regulation under the Telecommunications Law regarding, among other things:

licenses;

royalties and other payments to the government to be paid by licensees;

content and scope of programming;

the subscriber charges set by cable television operators for their cable television services;

our cable infrastructure that will become the public telecommunications network; and

the nature of telecommunications services.

Changes in laws, regulations or government policy affecting our business activities could adversely affect our business and operations. In the event that we notify the Council that we wish to reduce the scope of the Basic Package for analog subscribers, we may be instructed to reduce the price charged for such package. The Minister of Communications also has the authority to intervene and set minimum and maximum charges to our subscribers in the event that he determines that our charges are not reasonable, or are harmful to competition. We cannot assure you that the Minister of Communications will not intervene in relation to the amounts we charge our subscribers.

As a result of the changing regulatory environment we have lost the competitive advantage we previously enjoyed as a holder of exclusive franchises, and we face competition from a variety of sources. This has lowered the entry barriers for potential new competitors and may affect our ability to provide services to our subscribers.

The Israeli telecommunications market is in a state of transition, moving to a more liberalized environment in which various markets are being gradually opened to competition. Amendments to the Telecommunications Law replaced the previous system of exclusive franchises by general non-exclusive licenses. The licenses we have received (and the terms of the approvals we have received from the regulatory authorities with regards to the proposed merger between the Israeli cable television operators), have significantly reduced the barriers to entry to our market and impose conditions upon us that allow our competitors to access our subscribers.

In January 1999, the Ministry of Communications granted a license for the provision of television broadcasts to subscribers in Israel via satellite to D.B.S. Satellite Services (1998) Ltd., commonly known as YES . Bezeq Israel Telecommunications Corporation Ltd. is a controlling shareholding of YES. YES began to operate and market its broadcasts in July 2000. Bezeq is a government company, which has a monopoly over the provision of domestic fixed line telephony services, data transmission services, access to high-speed Internet and telecommunications infrastructure. Bezeq has great financial resources, which it may place at the disposal of YES, thereby allowing YES to offer its services at low prices and use aggressive marketing strategies with which we may not be able to successfully compete. We also have an obligation to lease our Inside Wiring to YES, and YES is under a reciprocal obligation to us, pursuant to directives issued by the Minister of Communications. Such competition from YES has affected our income, reduced the number of subscribers and caused us increased expenses, mainly in marketing and programming. In particular, the purchase power of YES has materially raised the cost of purchase of content from the major producer companies (namely Warner Brothers, Universal, Buena Vista, Paramount, MGM, Columbia and Twentieth Century Fox).

The Telecommunications Law, as amended, our Licenses and the terms of the approvals we have received to date from the regulatory authorities with regards to the proposed merger of the Israeli cable television operators, also impose upon us an unbundling obligation, the purpose of which is to encourage competition. The obligation both allows other broadcasting licensees access to our subscribers, through our network infrastructure, on terms that are not inferior to the terms provided by our Telecommunications Infrastructure Licensee to our Cable Broadcast Licensees; and also allows other telecommunications licensees (who may therefore be providers of, among other things, other value added services) to have access to our infrastructure. Further, pursuant to the terms of the approvals we have received in relation to the proposed merger between the Israeli cable television operators, in the event that the Controller considers there to be a material regression in competition in the multi channel television market we may be instructed to allow YES, or other broadcast licensees, usage of our network infrastructure to all potential subscribers, and not only to our subscribers, so long as our cable network infrastructure reaches their premises. (If YES ceases to operate due to insolvency, this will be deemed to be a material regression in competition in the multi channel television market and we may be instructed to allow YES or its successor usage of our network infrastructure as mentioned above).

Pursuant to our Licenses and the law, we are obliged to reserve and allow one sixth of our broadcasting network capacity for broadcasts of channels produced by special cable broadcast licensees to our subscribers. According to the Telecommunications Law, as amended, without derogating from the general unbundling obligation referred to above, and taking into account the said obligation with regards to reserving one sixth of our network capacity, the Minister has the authority to direct the Telecommunications Infrastructure Licensee to designate network capacity for the transmission of broadcast and other telecommunications services of a third party.

We cannot anticipate how and to what extent these obligations shall affect our income and expenses, or our subscriber base in the future.

We provide a service of access to High Speed Internet over cable, which faces significant competition.

Since April 2002, we provide a service of access to High Speed Internet over cable. We have incurred considerable capital expenditure preparing for the provision of this service and anticipate that we shall continue to invest in the improvement and maintenance of this service in the future. However, we face significant competition from the government owned Bezeq and may face competition in the future from other well placed competitors. There is no assurance of the level of return on our investments in this service.

We may face competition from other existing technologies in broadcasting and infrastructure that may be implemented in Israel, or new technologies that could reduce the appeal of our services.

While we believe that our existing technologies allow us to effectively compete with other existing technologies implemented in Israel, we may face competition from existing technologies that may be implemented in Israel. We cannot anticipate whether, and to what extent if at all, future changes in technology will materially affect the continued use of fiber optic and coaxial cabling technologies that we employ. We may also face competition from technologies in development or that may be implemented in the future, such as LMDS, wireless local loop in the fields of data over cable and telephony, and video on demand and personal video recorder (or PVR) services that may be deployed over digital subscriber line (or DSL) and satellite platforms. We cannot predict what will be the effect of existing, emerging and future technological changes on the viability or competitiveness of our system. Accordingly, we cannot assure you that the technologies we currently employ, or shall employ in the future, will not become obsolete or subject to competition from new technologies in the future.

The cable television industry is subject to regulation and antitrust review in respect of the programming offerings that it provides, which limits our ability to independently select programming, and causes us significant expenses and investments in the development of programming.

In 1989, together with the other two Israeli cable television operators, we established a company named I.C.P. Israel Cable Television Programming Company Ltd., or ICP , for the purpose of jointly purchasing and producing content for our local cable channels. Prior to the approval of the Controller of Restrictive Business Practices to the proposed merger of the Israeli cable television operators, the validity of ICP s activity was subject to the approval of both the Council and the Restrictive Business Practices Authorities. Under the approval of the Controller of Restrictive Business Practices to the proposed merger of the Israeli cable television operators, it is no longer necessary for the activity of ICP to be subject to the approval of the Restrictive Business Practices Court. Should the merger not be consummated, the activity of ICP shall continue to be also subject to the supervision of the Restrictive Business Practices Authorities.

The Council s approval to the activity of ICP, which has been extended a number of times, is subject to certain conditions, one of which is that the cable television operators allow YES to broadcast channels produced, under the ICP settlement by ICP or the independent producers (namely, family, sport, movies and children s channels) for consideration, during the approval period, with the exception of certain original local productions. These channels are among the most widely viewed channels in Israel. The obligation upon us to allow direct broadcasting of these channels by YES expires upon the earlier of either: December 31, 2003 (regarding the family, movie and sports channels), and March 1, 2003 (regarding the children s channel); or the date on which YES has at least 500,000 subscribers, after which YES may request an extension.The obligation regarding the children s channel has since expired. YES broadcasts the family channel produced by ICP. YES ceased to broadcast the movie channel produced by ICP on June 30, 2002. The terms and conditions of the approvals of the Council and Controller of Restrictive Business Practices to the proposed merger also impose significant restrictions on the activity of the merged entity in relation to all areas of our business, including programming, marketing and broadcasting.

The Council s approval of the activity of ICP, together with other Council decisions allowing us to broadcast local channels, obligated the cable television operators (including ourselves) to invest an aggregate sum of up to approximately $33.7 million per year in original local productions, each in proportion to each operator s relative share of the total number of cable television subscribers in Israel. Amendments to the Telecommunications Law stipulate that in place of such yearly obligation, investments in local productions should equal between 8% and 12% of the annual income of the cable television operators from subscription fees. Pursuant to these amendments, the Council has the authority to fix the percentage from the 8%-12% range, while taking into account the economic status of the cable television operators in the field of cable broadcasts. In accordance with the Council s decision of June 2002, as amended in September 2002 and May 2003, each Cable Broadcast Licensee is required to allocate to production or purchase of locally produced broadcasts, a percentage of its annual income derived from subscriber fees for the year preceding the year of the investment, as follows: (i) commencing April 30, 2002 (the date of the grant of the Cable Broadcast License) and until the end of 2005, at least 8% of such income; and commencing 2006 and thereafter, as to be determined by the Council prior to the end of June 2005; and (ii) in the event a Cable Broadcast License is granted to the merged entity of the Israeli cable television operators, the Council shall determine, prior to the end of June 2005, the rate of the amounts that shall be allocated to local productions by the Cable Broadcast Licensee as of 2006. For this latter purpose, the Council shall consider, among other things, the financial condition of the Licensees in connection with their broadcast activities and the contribution of the merger to the improvement of the financial condition of the Licensees.

Each of the Israeli cable television operators, including us, is also still under a continuing obligation, as set forth in our Cable Broadcast Licenses, to fulfill programming obligations which remain outstanding pursuant to the previous franchises, including the obligation to invest in local productions. According to our Cable Broadcast Licenses, we may notify the Council of our intention to remove certain channels from our Basic Packages and to transmit those channels within the Premium Broadcastings that we offer our digital subscribers in our tiering system. In such event, the Council has the authority to recommend to the Ministry of Communications that our analog subscriber fees for the Basic Package be reduced. This could have a material impact on our revenues, if the fees received from other sources do not compensate for the loss of such fees.

Our financial condition may be affected by the market price of one of the cellular telecommunications companies authorized to operate in Israel, in which we have invested.

We hold approximately 7.42% of the outstanding share capital of Partner Communications Company Ltd., the shares of which are publicly traded on the Nasdaq National Market, the London Stock Exchange and the Tel Aviv Stock Exchange, and Partner s debentures are listed for trade on the Luxembourg Stock Exchange. Partner holds a license to provide cellular telecommunications services in Israel, and is currently one of the two operators in Israel to use the global system for mobile telecommunications, or GSM, on a fully commercial basis, a comprehensive digital standard for the operation of all elements of a cellular telephone system. Partner faces intense competition from other cellular telecommunications service operators in Israel and the Palestinian operator, Jawaal, and also faces competition from fixed line operators in Israel, currently Bezeq Israel Telecommunications Corporation Ltd. The market price of Partner s shares has been and may continue to be volatile in response to conditions of the global securities markets in general and the communications and technology sectors in particular. The foregoing and other factors could cause the market price of Partner s shares to fluctuate unpredictably, and could adversely affect the market price of Partner s shares.

Partner s results are reflected in our financial statements through December 31, 2002 on an equity accounting basis and consequently have a material effect on our financial results. Approximately 72% of our current holdings in Partner are pledged to banks under pledges unlimited in sum, to cover Partner s liabilities in respect of its loans from the banks.

We cannot assure you that Partner will be able to successfully compete against existing or new competitors in the field of cellular telecommunications, or that Partner s systems and business plan will be adequate, efficient and capable of performing in light of the large number of material factors that may affect its future operations and prospects.

We may incur expenses in connection with our shareholdings in an Israeli international telecommunications service provider.

We hold a 10% share ownership interest in Barak I.T.C. (1995) The International Telecommunications Services Corp. Ltd., which holds a license to provide international telecommunications services in Israel. Barak competes with two other licensed international telecommunications service providers, and two additional substantial Internet service providers. One of these competitors is Bezeq International Ltd., which is a subsidiary of the domestic telecommunications service provider, Bezeq Israel Telecommunications Corporation Ltd., which until recently had a sole monopoly. As a result of this connection, Bezeq International Ltd. has stronger name recognition, long - standing customer relations, and significantly greater financial and technical resources than the other competitors in the international telecommunications market, including Barak.

Users of international telecommunications services may subscribe for the services of any provider in Israel, and may change their choice, at any time. In addition, a user may select the services of any of the providers on a call-by-call basis. As a result, regular subscribers of Barak may not necessarily use Barak services exclusively.

The Israeli government may grant additional licenses for the establishment and operation of international telecommunications systems in Israel. Such competitors may be larger than Barak or have greater financial resources, better technology or services, and Barak may not be able to successfully compete with them. This may have the impact of reducing Barak s market share. Furthermore, the international telecommunications market is characterized by rapidly changing technology and customer requirements, new industry standards and frequent new product and service introductions. If Barak is unable to anticipate and keep pace with these changes, it may lose market share. Barak s performance or market penetration might not be enhanced and our investment in Barak might not be fruitful.

We are controlled by a small number of shareholders.

At May 31, 2003, our principal shareholders were the beneficial owners of approximately 80% of our outstanding ordinary shares. Our principal shareholders except Ma ariv Modein Publishing House Ltd. are parties to a shareholders agreement, which relates to, among other things, the election of our directors. Subject to applicable law and the provisions of the shareholders agreement, our principal shareholders have the ability to determine the election of all of our directors, and to direct our policies, including the payment of dividends, and can control the outcome of substantially all matters that may be brought before our shareholders.

We may not be able to obtain additional capital in order to implement our business plans on favorable terms, and may have a dilutive effect on our shareholders.

Our existing capital resources may not be adequate to satisfy our financial needs in order to implement our business plans, for the next 12 months. Our financial needs in that period will be subject to, among other things: our ability to successfully provide our services; the need to upgrade our network to provide added value services; the need to implement the buildout of our infrastructure in peripheral areas; and the needs of companies in which we have significant investments, such as Partner, Barak and, if the proposed merger shall be consummated, the merged entity.

Any future equity or debt financing, if available, may be on terms that are not favorable to us, and in the event of equity financing, could result in dilution of our shareholders interests. Although our principal shareholders have made loans and contributed equity to us in the past, they are not contractually obligated to do so in the future.

We commenced negotiations with the banks regarding an increase of our credit lines. These negotiations were ceased due to the proceedings in connection with the proposed merger of the Israeli cable television operators, however we may recommence these negotiations depending on the progress of the merger or should the merger proceedings cease to continue. Should we recommence such negotiations, there is no assurance that we shall reach an agreement with the banks and receive such increased credit lines. In the event that we are granted increased credit lines to meet our financial needs, there can be no assurance that we would be able to obtain terms which are favorable to us, or which are not significantly expensive, in light of current market conditions.

Our industry is subject to rapid technological changes that will cause us to incur capital expenditures in order to remain competitive.

In order to provide advanced communication services, we have incurred significant capital expenditures expanding the cable network bandwidth from 550 MHz to 860 MHz. We have a technological advancement plan for deployment of additional two-way services, expansion of fiber optic cable networks and a digital broadcasting system or advanced data over cable platform. We also aim to improve the network in terms of redundancy and manageability, by closing fiber rings, enhancing the powering and telemetry measures, and downsizing the fiber nodes. Such enhancements are necessary to allow us to provide telecommunication services at a Telco-Grade quality of service, which is the standard commonly used by telephone companies to grade availability and quality of services.

Our business may be impacted by the shekel exchange rate fluctuations and inflation.

Our financial statements are presented in shekels, adjusted to reflect changes in the Israeli consumer price index. Consequently, all shekel amounts set forth in our historical financial statements are adjusted each time that we publish new financial statements in order to reflect changes in the Israeli consumer price index as of the date of the latest balance sheet presented. See Note 2 to the financial statements. Since we may be unable, or not permitted to raise our rates and fees pursuant to our Licenses in a manner that would fully compensate for any increase in the Israeli consumer price index, inflation in Israel may have a material adverse impact upon us. Our financial expenses are also affected by inflation, such that high rates of inflation cause a decrease in the real value of our unlinked assets, which in turn, causes an increase in our financial expenses. Likewise, high rates of inflation cause a decrease in the real value of our unlinked liabilities, which in turn, causes a decrease in our financial expenses.

Substantially all of our revenues and a minority of our operating expenses are denominated in shekels, and on the other hand, substantially all of our programming expenses, certain other expenses and most of our capital expenditures are denominated or linked to foreign currency. Thus, any devaluation of the shekel against the US dollar (or other foreign currencies), will also increase the shekel cost of our non-shekel denominated or linked expenses. Such increase may have an adverse impact upon our operating results, which may be material. Our borrowings are mostly in Israeli shekels.

Our ordinary shares and ADSs are listed for trading on different markets and this may result in price variations.

Our ordinary shares are listed for trading on the Tel Aviv Stock Exchange, or TASE, and our ADSs are listed for trading on the Nasdaq Stock Market, or Nasdaq. Each ADS represents two ordinary shares. Trading in our ordinary shares and ADSs on these markets is made in different currencies (US dollars on Nasdaq and NIS on TASE), and at different times (resulting from different time zones, different trading days and different public holidays in the United States and Israel). Actual trading volume on Nasdaq or the TASE could be insignificant and as such could be subject to volatility. The trading prices of our ordinary shares and ADSs on these two markets often differ, resulting from the factors described above, as well as differences in exchange rates. Any decrease in the trading price of our ordinary shares on the TASE could cause a decrease in the trading price of our ADSs on Nasdaq, and any decrease in the trading price of our ADSs on Nasdaq could cause a decrease in the trading price of our ordinary shares on the TASE.

We are subject to the political, economic and military conditions in Israel.

We are incorporated and based in, and currently derive almost all our revenues from markets within, the State of Israel. As a result, the political, economic and military conditions in Israel directly influence us. Hostilities involving Israel, the interruption or curtailment of trade between Israel and its trading partners, political instability within Israel or its neighboring countries, a significant downturn in the economic or financial condition of Israel and changes in Israeli laws and regulations, including taxation, are likely to cause our revenues to fall and harm our business.

Since the establishment of the State of Israel in 1948, a number of armed conflicts have taken place between Israel and its Arab neighbors and a state of hostility, varying from time to time in intensity and degree, has led to security and economic problems for Israel. Since October 2000, there has been an increased level of hostilities and violence between Israel and the Palestinians, which has adversely affected the peace process and has negatively influenced our relationship with several Arab countries. The future effect of this deterioration and violence on the Israeli economy and our operations is unclear. From time to time Israeli companies or companies doing business with Israeli companies have been subject to an economic boycott initiated by several Arab countries. This boycott or similar restrictive laws or policies directed towards Israel or Israeli business could adversely affect us. Ongoing violence between Israel and its Arab neighbors and Palestinians, or any other hostilities involving or threatening Israel, may have a material adverse effect on our business, financial condition or results of operations.

Due to, principally, a continuing budget deficit of the Israeli government and the slow down of the Israeli economy in recent years, the Israeli parliament approved, on May 29, 2003, an economic plan that entails, among other things, budget cuts in various sources of government spending, the increase of various tax liabilities and cuts in various social benefits. It is not known at this stage what impact the implementation of the approved economic plan would have on the Israeli economy. Since we are located in, and currently derive almost all our revenues from markets within Israel, economic events in Israel, or uncertainties associated with such events, could adversely affect our operations and financial results.

Some of our directors, officers and employees are currently obligated to perform annual reserve duty. Generally, male adult citizens and permanent residents of Israel under the age of between 45 and 50, unless exempt, may be required to perform up to approximately 36 days of military reserve duty annually. Certain reserve soldiers may be required to serve more. Additionally, all such reservists are subject to being called to active duty at any time under emergency circumstances. While we have operated effectively under these requirements since we began operations, we cannot assess the full impact of these requirements on our workforce and business if conditions should change, and we cannot predict the effect of any expansion or reduction of these obligations on us.

Provisions of our Licenses and Israeli law could delay, prevent or make difficult a merger or acquisition or a change of control of us and therefore depress the market price of our shares.

Our Cable Broadcast Licenses, Infrastructure License and HeadEnd License include restrictions regarding changes of means of control of the Licensees.

The Israeli Companies Law generally requires that a merger be approved by a company s board of directors and by a majority of the shares voting on the proposed merger. Unless a court rules otherwise, the statutory merger will not be deemed approved if a majority of the ordinary shares held by shareholders other than the potential merger partner (or by any person who holds 25% or more of the shares of capital stock or the right to appoint 25% or more of the directors of the potential merger partner) vote against the merger. Upon the request of any creditor of a party to the proposed merger, a court may delay or prevent the merger if it concludes that there is a reasonable concern that, as a result of the merger, the surviving company will be unable to satisfy its obligations. In addition, a merger may not be completed unless at least 70 days have passed since the filing of the merger proposal with the Israeli Registrar of Companies.

In certain circumstances an acquisition of shares in a public company must be made by means of a tender offer if, as a result of the acquisition, the purchaser will become a 25% or 45% shareholder of the company (unless there is already a 25% or a majority shareholder of the company, respectively). If, as a result of an acquisition, the acquirer will hold more than 90% of a company s shares, the acquisition must be made by means of a tender offer for all of the shares. The described restrictions could prevent or make more difficult to acquire us, which could depress our share price.

Additionally, Israeli tax law treats some acquisitions, such as stock-for-stock exchanges between an Israeli company and a foreign company less favorably than U.S. tax laws. For example, Israeli tax law may, under certain circumstances, subject a shareholder who exchanges his ordinary shares for shares in another corporation to taxation prior to the sale of the shares received in such stock-for-stock swap.

These provisions of our Licenses and of the Israeli corporate and tax law (and the uncertainties surrounding such laws) may have the effect of delaying, preventing or making more difficult a merger or acquisition or change of control of us, and depress the market price of our ordinary shares which otherwise might rise as a result of such a change of control.

It may be difficult to (i) enforce a U.S. judgment against us, our officers and directors and our Israeli auditors, (ii) assert U.S. securities laws claims in Israel, and (iii) serve process on substantially all of our officers and directors and these accountants.

We are incorporated in Israel. Substantially all of our executive officers and directors and our Israeli auditors are nonresidents of the United States, and a substantial portion of our assets and the assets of these persons are located outside the United States. Therefore, it may be difficult for a shareholder or holder of our ADS s, or any other person or entity, to enforce a U.S. court judgment based upon the civil liability provisions of the U.S. federal securities laws in an Israeli court against us or any of those persons or to effect service of process upon those persons in the United States. Additionally, it may be difficult for a shareholder or holder of our ADS s, or any other person or entity, to enforce civil liabilities under U.S. federal securities laws pursuant to original actions instituted in Israel.

We and the other cable television operators have agreed on the terms of a merger. The merger might not be consummated, and if it is, we might not be able to realize any anticipated benefits from the merger.

In February 2003, we and the other Israeli cable television operators agreed on a final version of an agreement outlining the structure and conditions of a merger between us and the other Israeli cable television operators and their subsidiaries (further to previous arrangements between the parties). This merger agreement, upon its signing, will be added to and broaden the terms of the previous arrangement between the parties executed on December 31, 2001 (further to previous arrangements between the parties that were cancelled and replaced). In the event any terms of these agreements shall conflict, the terms of the latter agreement of February 2003 shall prevail. To date, the final merger agreement has not been signed.

Prior to the merger we will need to reach an understanding with the major Israeli banks, which are creditors of the parties to the merger. The merger must also receive approvals under applicable law, including the approvals of the Council, the Income Tax Commission, the Controller of Restrictive Business Practices, and by the Israeli court, after receiving the approvals of certain creditors and the relevant corporate bodies of the relevant parties. To date, approvals have been granted, subject to terms and conditions, from the Council, the Controller of Restrictive Business Practices and the Income Tax Commission. Subject to the final terms of the merger, further approval of the Income Tax

Commission to the merger may be required. One of the issues outstanding to date in connection with the consummation of the merger is regarding the position of the Supervisor of the Banks of the Bank of Israel in connection, among other things, with the matter of certain limitations under Israeli banking laws.

The objectives of the merger are, among other things, to enable the merged company to provide additional telecommunications services, to increase our ability to effectively compete with Bezeq Israel Telecommunications Corporation Ltd., and to effect substantial cost savings. There can be no assurance that the merger will be consummated. In the event that the merger is not consummated, it will be more difficult to realize these objectives and to compete. In addition, should the merger not be consummated, our operating expenses and marketing expenses may increase, since we may no longer benefit from reduced programming and advertising costs, which result from the current joint purchase of content and joint advertising campaign of the three Israeli cable television operators.

If the merger is consummated, there can be no assurance whether: (i) the conditions of the merger will enable the merged entity to successfully compete; (ii) there will be a successful integration between the merged entities; and (iii) the combined entity will be able to compete effectively against current or future competitors and will realize the anticipated benefits of the merger.

If the merger is consummated, we face the following risks:

We are indirectly controlled by certain members of the Dankner family, who also own indirectly 11.63% of Bank Hapoalim Ltd.,the largest bank in Israel, and which constitute part of the controlling group of Bank Hapoalim Ltd., which own approximately 45.18% of the Bank. We are consequently subject to restrictions under Israeli banking laws concerning credit, consents and limitations with Bank Hapoalim. The restrictions to which we are subject may therefore apply to the merged entity. Additionally, Bank Hapoalim is a creditor of the other companies who are parties to the proposed merger, and will therefore be a creditor of the merged entity.

As a result of the merger, we may be characterized as a passive foreign investment company, and as a result our U.S. shareholders may suffer adverse tax consequences. Generally, if for any taxable year 75% or more of our gross income is passive income, or at least 50% of our assets are held for the production of, or produce, passive income, we may be characterized as a passive foreign investment company for U.S. federal income tax purposes. This characterization could result in adverse U.S. tax consequences to our shareholders, including having gain realized on the sale of our shares be treated as ordinary income, as opposed to capital gain income, and having potentially punitive interest charges apply to such sales proceeds. U.S. shareholders should consult with their own U.S. tax advisors with respect to the U.S. tax consequences of investing in our ordinary shares.

As a result of the merger, we may be deemed to be an investment company under the Investment Companies Act of 1940. A significant part of our assets may constitute investment securities as defined in the Investment Company Act. If we were deemed to be an investment company, then we would be required to be registered as such. In that case there would be a substantial risk that we would be in violation of the Investment Company Act because of the practical inability of a non-U.S. company to register under the Investment Company Act. If we were deemed to be an unregistered investment company under the Investment Company Act, our contracts may be voidable, we might not be allowed to offer securities in the United States, and we may also be subject to other materially adverse consequences.

The sums that will be deemed to have been borrowed by the merged entity may exceed the maximum borrowing limit of a single borrower under the Israeli banking laws, which might materially restrict the ability of the merged entity to receive loans from Israeli banks. In addition, we, the merged entity and the other parties to the merger may be subject to additional limitations with connection to receipt of loans from Israeli banks due to restrictions under Israeli Banking laws pertaining to the maximum borrowing by a group of borrowers.

The goodwill contributed to the merged entity by the merging entities could result in accounting expenses under Israeli GAAP in the years following the consummation of the merger that would reduce our shareholders equity and would have an adverse effect on the public market for our shares and ADS s, and negatively affect our ability to pay dividends to our shareholders. A material reduction in our shareholders equity could cause our shares to be delisted from the Tel Aviv Stock Exchange and Nasdaq National Market.

For the merger, including certain ancillary actions performed in the framework of the merger, to qualify, pursuant to the approval of the Israeli Income Tax Commission to the merger, as a tax-free transaction under Sections 103, 104 and 105 of the Israeli Income Tax Ordinance, the merging entities and their respective shareholders (including us) are required to comply with certain restrictions until December 31, 2003, including restrictions on certain issuances of shares of the merged entity and restrictions on the number of shares that may be sold by the shareholders of the merged entity. In addition, the merged entity may not sell a majority of the assets (as defined in the Income Tax Ordinance) transferred to it by the merging entities during this restricted period, and no actions, transfers, provision of guarantees or any other activities may be performed between the merged entity and the other entities that participated in the merger, including their respective shareholders. In the event that any of these conditions or restrictions are not complied with, the tax exemption may be retroactively cancelled and the merger may be subject to tax, plus a consumer price index linkage adjustment and interest. These restrictions may deter an acquisition of the merged entity, and prevent us from selling or disposing of our shares in the merged entity. Additionally, subject to the final terms of the merger, further approval of the Income Tax Commission to the merger may be required and additional conditions or restrictions may be imposed on the merged entity, the merging entities and their respective shareholders.

The terms and conditions of the approvals that we have received to date to the merger affect the ability of the merged entity to manage its business, and restrict the ability of the merged entity to utilize any potential competitive advantage it may otherwise have.

In the event that the Controller of Restrictive Business Practices considers there to be a material regression in the multi channel television market as a result of the consummation of the merger, he has the power to oblige the merged entity to allow other broadcast license holders (including YES) usage of the network infrastructure to access all potential subscribers, and not only to the subscribers of the merged entity.

A condition of the approval of the Controller of Restrictive Business Practices to the merger is an obligation upon the merged entity to begin to supply fixed line telephony services over cable infrastructure to the Israeli public within a year of receipt of its infrastructure license and no later than two years of the date of the approval. The merged infrastructure entity is obligated to invest in fixed line telephony cable infrastructure an aggregate of not less than NIS350 million, to be completed in accordance with predetermined stages throughout 2002 to 2005, as set forth in the approval. To date, we are unable to anticipate exactly how much our pro rata portion of such investment obligation will be.

The approval of the Controller of Restrictive Business Practices to the merger is conditional upon the provision of a bank guarantee in the amount of $15 million to ensure compliance with the terms of the approval. In the event that the Controller of Restrictive Business Practices decides, in his discretion, that there has been a material breach of the terms of the approval, he may fully exercise the guarantee. We have provided our pro rata portion of this guarantee, in the amount of $3.75 million.

The financial situation of the other Israeli cable television operators has an impact upon our business.

On April 22, 2002, Tevel Israel International Ltd., one of the other Israeli cable television operators filed a motion for stay of proceedings, which is one of the procedures available to an insolvent company in Israel. The stay of proceedings was granted by the Court on April 23, 2002, and is currently valid until July 2, 2003. The Court appointed a Trustee for the duration of the period of the stay of proceedings. The legal implication of the stay of proceedings, is that it is not possible for a claim to be brought against Tevel during the period of the stay, and all past debt incurred by Tevel prior to April 22, 2002, shall be dealt with in accordance with a creditors arrangement to be proposed by the Trustee, assuming that such credit arrangement shall be approved by the Court. The Trustee is responsible, among other things, for the management of Tevel during the period of the stay. The approval of the Court is required in order for Tevel to participate as a party to the merger.

The current financial situation of Tevel, and any possible future deterioration of Tevel, has an impact upon our business and our day to day operations, including causing an increase in our respective pro rata portion of costs of content, which may have a material adverse affect upon our financial statements. Further, it may affect the possibility of the consummation of the proposed merger between the Israeli cable television operators, and the conditions that the creditors of the companies that are parties to the merger may impose.

Our previous franchises required us to meet certain milestones with respect to cable access to potential customers in the areas covered by our Licenses, which if not met, could expose us to litigation or administrative actions.

Our previous exclusive franchises contained specific construction milestones with respect to regions within a franchise area that must be passed by the cable television network by specified dates. We substantially completed the installation of the regional cable transmission network in all our operating areas, and believed that completing portions of the buildout requirements in peripheral regions in the operating areas would be substantially more expensive, on a per-subscriber basis than in the metropolitan areas. Therefore we did not fully complete buildout requirements in certain peripheral regions. Our current Licenses require us to connect any applicant to purchase cable television broadcasts within 14 days, from the application date, and in the event that the network does not reach an applicant s premises, within 3 months. The Ministry of Communications or exceptional committee may allow an exception regarding the time schedule to connect applicants, or the obligation to connect every applicant.

We are subject to a lawsuit and have been subject to other lawsuits in the past, and may be exposed to additional lawsuits in the future, by residents of communities that are not, or were not, connected to the cable television network, seeking to force us to implement the build-out of our network in their communities, or compensation for being prevented from receiving cable television services. See Item 8A. Consolidated Statements and Other Financial Information - Legal and Arbitration Proceedings .

We face intense competition, which may intensify in the future and impede our ability to regain profitability.

Increased competition in the multi channel television market in recent years has caused, among other things, a rise in costs, especially programming costs, a reduction in our revenues resulting from loss of subscribers, and an inability to raise our subscriber fees. This has contributed to our losses for the years 2000, 2001 and 2002. There is no assurance that we will be able to regain profitability in the foreseeable future, especially in an increasingly competitive environment.

Our substantial leverage could adversely affect our financial health.

In the years 2000, 2001and 2002, we incurred intensive capital expenditures related to the continued construction of our cable television network and other technological projects, and operating losses, which have increased our indebtedness, resulting in our becoming significantly highly leveraged.

Our ability to meet our debt obligations will depend on whether we can successfully implement our strategy, as well as on financial, competitive, regulatory and technical factors, including some factors that are beyond our control. If we are unable to generate sufficient cash flow from operations to meet principle and interest payments on our debt, we may have to refinance all or part of our indebtedness.

We cannot assure you that any such refinancing would be possible on terms that we could accept or that we could obtain additional financing. If refinancing were not possible or if additional financing were not available, we may have to sell our assets under circumstances that might not yield the highest prices, or default on our debt obligations.

ITEM 4. INFORMATION ON THE COMPANY

4A. History and Development of the Company

We were incorporated in Israel under the laws of the State of Israel on June 28, 1987. Our principal executive offices are located at 42 Pinkas Street, North Industrial Area, Netanya 42134 Israel (telephone: 972-9-860-2160). Our website address is www.matav.co.il. Our agent for service of process in the United States is Puglisi & Associates, 850 Library Avenue, Suite 204, P.O. Box 885, Newark, Delaware 19715.

We are one of three operators and providers of broadband cable television services in Israel. Our cable television services are marketed under the name Matav Digital .

Prior to the grant of our licenses in 2002, we operated pursuant to five exclusive franchises granted to us by the Ministry of Communications to provide cable television services in franchise areas, which covered approximately 25% of Israel s households. As of December 31, 2002 we provided cable television services to approximately 26% of all cable television subscribers in Israel. We own substantially all of our cable television network infrastructure. Our exclusive franchises covered four operating areas, three of which included the major metropolitan areas of Bat-Yam Holon, Haifa, and Netanya Hadera, and one of which served the less densely populated area of the Galilee. Our subscriber penetration is highest in the metropolitan operating areas.

We began serving cable television subscribers in 1990. The total number of our cable television subscribers was approximately 286,600 on December 31, 1999, in comparison to approximately 275,000 as of December 31, 2002. Cable television subscriber penetration has decreased by approximately 11.0% during the same period. Since April 2002, we offer a commercial service of access to High Speed Internet over cable, pursuant to our Telecommunications Infrastructure License. Our aggregate revenue has increased from approximately NIS 490.7 million on December 31, 1999 to approximately NIS 505.0 million as of December 31, 2002 (including revenue from cable television and access to High Speed Internet subscribers). During the same period, our operating income and net income has decreased from approximately NIS 117.2 million and net income of approximately NIS 340.5 million for the year ended December 31, 1999 to an operating loss of approximately NIS 100.6 million and net income of approximately NIS 34.5 million for the year ended December 31, 2002. EBITDA has decreased from approximately NIS 207.2 million for the year ended December 31, 1999 to approximately NIS 57.8 million for the year ended December 31, 2002.

Through December 31, 2002 we have invested approximately NIS 2025.2 million (approximately US$ 427.5 million) in the build-out of our cable television network within our license areas and in other fixed assets.

We operate both directly and through subsidiaries in various fields of telecommunications. We have adopted a growth strategy that combines core activities in the multi-channel television market, based on state-of-the-art technology, with the use of cable television infrastructure. We are able to provide data over cable and other supplementary services.

We have expanded our telecommunications activities by investing in Barak I.T.C. (1995) The International Telecommunications Services Corp. Ltd., an international telephony service provider in Israel, and in Partner Communications Company Ltd., the third of four licensed providers of mobile cellular telephone services in Israel, and one of the two providers using the global system for mobile telecommunications, a comprehensive digital standard for the operation of all elements of a cellular telephone system, known as GSM.

Until April 2002, we beneficially held approximately 15.2% of Partner s issued and outstanding shares. Pursuant to the sale of approximately half of our shares in Partner in April 2002, we are now the beneficial owners of approximately 7.42% of Partner s issued and outstanding share capital.

We, together with other of our shareholders, formed Nonstop Ventures Ltd. for the purpose of investing in start-up companies, which engage in the fields of Internet, cable television, data telecommunications, applications, content, infrastructure and Internet Protocol telephony. As of November 2002, we own 50% of the issued share capital of Nonstop Ventures.

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Important events in the development of the cable television and telecommunications industry, and our business

Overview

Television broadcasting in Israel began in 1967 through one off-air government controlled channel, known as Channel 1. In 1993, private operators commenced regular commercial broadcasts of a second off-air channel, known as Channel 2, and later, a further channel, the Israeli Knesset Channel (Channel 33). In April 2000, the Ministry of Communications approved the establishment of a second commercial channel (Channel 10), which began broadcasting at the beginning of 2002.

During the early 1980 s, several unlicensed operators installed cable television systems in limited areas throughout Israel. In 1986, the Telecommunications Law was amended to restrict transmission of television broadcasts by cable other than pursuant to licenses granted by the Ministry of Communications under the Telecommunications Law.

In 1989, we, together with the other cable television operators, formed I.C.P. Israel Cable Programming Company Ltd., or ICP , for the purpose of jointly purchasing and producing our local cable channels, which then consisted of four channels: family, movies, sport, and children. The culture & science channel was later added. Today, ICP creates, produces and acquires content for only two channels (family and movies), and independent producers produce the other three channels in accordance with the Restrictive Business Practices Court decision in 1996 regarding the ICP settlement (as extended).

In 1990, the Ministry of Communications began issuing exclusive franchises to operate cable television systems in various geographical areas in Israel. Each franchise paired a densely populated metropolitan area with a less densely populated rural area to ensure that smaller rural communities would also receive cable television services. The construction of the nationwide cable television network infrastructure began in late 1989 and, based on the number of homes passed with cable infrastructure, approximately 93% of the our network had been completed by at the end of 2002.

Pursuant to amendments to the Telecommunications Law in 2001 the exclusive franchises were replaced by a system of general non exclusive long term broadcast licenses, broadcasting HeadEnd licenses, and general non exclusive telecommunications infrastructure licenses, all of which we have been granted.

Direct Broadcasting by Satellite and Developments regarding YES

On January 5, 1998, the Israeli parliament approved an amendment to the Telecommunications Law, allowing the Ministry of Communications to give licenses for distribution of direct broadcast by satellite (DBS) services to subscribers. The Ministry of Communications granted D.B.S. Satellite Services (1998) Ltd., or YES , a license for the provision of television broadcasts to subscribers via satellite, and YES commenced DBS broadcasting in July 2000. The development of competition to cable television services from the commencement of DBS broadcasting has adversely affected our business. Following a dispute arising out of the grant of the license to YES, and recognition by the government of our ownership of the cable television network infrastructure, the cable television operators entered into an agreement with the State of Israel dated July 2001, in which the cable television operators, including us, undertook not to bring any claim in the future regarding the grant of a license to YES, and to make certain payments to the government over a 12 year period, commencing January 1, 2003. In consideration, we received recognition by the government of our ownership of the cable television network infrastructure.

On September 13, 2000, we, together with the other Israeli cable television operators, entered into an agreement with YES, under which we and the other cable television operators granted YES a non-exclusive permit to use our Inside Wiring for the transfer of satellite broadcasts (multi-channel television and interactive channels only); and YES granted the cable television operators a non-exclusive permit to use its Inside Wiring for the transfer of cable television broadcasts (including any other service provided by the cable television operators). This agreement has since been terminated by YES, and, in place of that agreement, in September 2001 the Minister of Communications issued administration directives, which were amended effective as of February 3, 2002, governing the reciprocal use of Inside Wiring between the cable television operators and YES. The directives establish instructions regarding the procedures of transition of cable television subscribers to become subscribers to YES and vice versa. These directives also provide that YES shall pay monthly fees to the relevant cable television operators for the use of their Inside Wiring, and that the cable television operators will pay fees to YES for the use of its Inside Wiring. The directives stipulate what such amounts should be. In addition the Minister of Communications has the authority to issue directives regarding the common use of the Inside Wiring by both YES and by the cable television operators, with regard to the provision of different services by each party. The Ministry of Communications conducted a hearing regarding the common use of Inside Wiring. To date, the Ministry has not issued directives regarding this matter.

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In addition, the Telecommunications Law, as amended, permits a person, in residential premises, to purchase from the Licensee the Inside Wiring installed in his premises.

Digital Broadcasting

We commenced digital broadcasting in July 2001, pursuant to approvals from the Council and the Ministry of Communications. These approvals allowed us to broadcast in a digital format our analog basic package channels and Pay-Per-View services, as well as other channels that have been subsequently approved for digital broadcast. These approvals include authorization to provide electronic program guide services, commonly referred to as EPG services .

We informed the Ministry of Communications that we would provide digital set-top boxes to our subscribers according to actual demand as follows: up to 100,000 set-top boxes will be provided in 2001; 70,000 in 2002, and 60,000 in 2003. The remainder is to be provided during the year 2004. As of May 2003, we have provided approximately 189,000 set-top boxes to our subscribers. We have already purchased approximately 210,000 set-top boxes (including 6,000 one way only set-top boxes). In October 2002, we and our subsidiary Cable Systems Media Haifa - Hadera Ltd. entered into a Term Sheet with Advent Digital Broadcast Ltd., a company incorporated in the British Virgin Islands, pursuant to which we will purchase 40,000 digital set-top boxes, to be provided in four equal portions, commencing December 1, 2002, and until August 1, 2003, for a total purchase price of $5.2 million. To date, 20,000 digital set-top boxes have been purchased from Advent Digital Broadcast Ltd. The Term Sheet shall bind the parties until such time that they shall enter into a definitive agreement. A definitive agreement has not been signed to date.

Tiering

On May 10, 2001, we received from the Council the approval to provide digital broadcasting services in a tiering system. The original approval included only a few channels. To date, most of the channel packages and other channels for which we requested approval by the Council have been approved, and services according to the tiering system began in July 2001.

As of December 2002, we and the other two Israeli cable television operators offer unified tiering packages, in the framework of which we changed the structure of the tiering packages we offer to our digital subscribers and the channels included in such packages. For a list of our channels and packages and the combinations of packages we offer as part of our tiering system, see Item 4B. Item 4B: Products and Services - Premium Broadcastings .

Pay-Per-View and Near Video on Demand

We began offering Pay-Per-View services in October 2000. We received from the Ministry of Communications a permit to provide Near Video On Demand services in the digital platform, although we have not yet begun to offer these services to our customers. Pay-Per-View and Near Video On Demand services are governed by our Cable Broadcast Licenses.

Internet Services

In 1999, we commenced specific operations targeted to the provision of access to High Speed Internet over cable services. However, at that time, we had not received the required license for providing such services, and therefore decided that we should provide Internet services (as an Internet service provider) using simple dial up access. We received a license to provide ordinary dial up Internet services in February 2000, and we commenced such services in April 2000. In parallel, we began to offer our subscribers access to High Speed Internet over cable on a trial basis, pursuant to a trial license.

On November 6, 2000, the Ministry of Communications granted Bezeq a license to supply High Speed Internet services using ADSL technology. Since, at that time, we had not received a license to supply access to High Speed Internet over cable services as a licensed Internet service provider, we decided to provide Internet services via Bezeq s ADSL. By April 2001, we had reached a share of approximately 20% of the Internet services market.

In May 2001, due to the fact that, among other things, we had not received the required license for providing access to High Speed Internet over cable services, we decided to cease our Internet operations. On June 3, 2001, we entered into an agreement with Bezeq International Ltd., an Israeli Internet service provider, and a subsidiary company of Bezeq, whereby Bezeq International would supply dial-up Internet services to our paying customers, other than those customers participating in the access to High Speed Internet over cable trial, and they will cooperate so that these customers will become customers of Bezeq International. Pursuant to the agreement with Bezeq International, 16,000 of our Internet dial up customers were transferred to Bezeq in consideration of $1.25 million.

The access to High Speed Internet over cable trials were continued during 2000, 2001 and the first quarter of 2002. On March 27, 2002, we received our Telecommunications Infrastructure License, which allows us to provide, among other things, access to High Speed Internet over cable services. After receipt of our Telecommunications Infrastructure License, the trials were discontinued and we began to offer (including to subscribers of the trial services) our commercial service of access to High Speed Internet over cable, which we launched on April 8, 2002. As of May 31, 2003, we provide access to High Speed Internet over cable services to approximately 33,000 subscribers.

Ownership of Cable Infrastructure and Payments to the State of Israel

In light of the contention of the Ministry of Finance according to which, following the expiration of the cable television operators franchises, the cable television operators should pay the State of Israel an appropriate consideration for the grant of a right to continue to provide multi channel television services to subscribers, as well as other telecommunications services over the cable network, under the licensing regime, the cable television operators, including ourselves, came to an agreement with the State of Israel dated July 2001, in which we undertook, among other things, to make certain payments to the government over a 12 year period, and in consideration, each cable television operator received recognition by the government of ownership of its respective cable television network infrastructure. Subsequent amendments to the Telecommunications Law adopted that payment arrangement. The material terms of the agreement provided that:

Each cable television operator shall make payments to the government over a period of 12 years commencing on January 1, 2003, equal to its pro rata portion of a sum determined by multiplying certain accumulated income of all the cable television operators, including certain income derived from the use of cable infrastructure, by a percentage which is between 0% and 4%, increasing gradually according to the amount of the certain income. In the July 2001 agreement, it was agreed that our pro rata portion would be 24.1%, until agreed differently by all of the cable television operators; and

Each cable television operator shall pay the State of Israel in the 12-year period up to 12% of its income from the sale of any activity related to the cable infrastructure or a right related to such activity, and the sale of certain assets as set forth in the agreement. The Israeli government (subject to payment of payments by the cable television operators) undertook not to assert any rights or claims regarding the ownership of the cable infrastructure.

As a result, each cable television operator is deemed to own all the rights regarding the cable network infrastructure in its license areas, and the right to operate it is subject to applicable law, following the expiration of the previous franchises. The terms of our Telecommunications Infrastructure License stipulate that upon termination of the Telecommunications Infrastructure License, in the event that we are unable to reach an agreement with a potential purchaser of our infrastructure within 6 months, then an arbitrator shall be appointed who shall impose a valuation calculated according to the value of the infrastructure, on a going concern basis and according its economic value.

The July 2001 agreement, and its codification into law due to the amendments to the Telecommunications Law, shall continue to be in effect if the cable television operators consummate the merger.

In March 2003 the cable television operators approached the Israeli Ministry of Finance with a request to defer for one year the commencement of payments due under the July 2001 agreement, and this matter is currently under discussion. In a meeting with the Israeli Ministry of Finance on April 30, 2003, the Ministry of Finance demanded that should the merger of the Israeli television operators be consummated, the July 2001 agreement will be adjusted to correspond with the new organizational structure following the merger, such that the merged cable infrastructure entity shall also become a party to the July 2001 agreement, and the provisions of such agreement regarding the proportional amounts of the cable television operators in the joint consideration to be paid to the State of Israel under such agreement shall be adjusted such that the merged cable broadcast entity and the merged infrastructure entity shall be severally and jointly responsible for the entire joint consideration due under such agreement.

Proposed Merger of the Israeli Cable Television Operators

In February 2003, the other Israeli cable television operators and us agreed on a final version of an agreement outlining the structure and conditions of a merger between us and the other Israeli cable television operators. This merger agreement, upon its signing, will be added to and broaden the terms of the previous arrangement between the parties executed on December 31, 2001 (further to previous arrangements between the parties that were cancelled and replaced). The purpose of the merger, among other things, is to enable us to provide additional telecommunications services, to increase our ability to compete successfully with Bezeq in the domestic fixed line telephony field, to cooperate in various areas, including purchase of content, marketing, sales and unified networks and effect substantial cost savings. The consummation of the merger agreement is subject to reaching an understanding with the major Israeli banks and the other creditors of the merging entities, and approvals required under applicable law, including the approvals of the Income Tax Commission, the Council, the Controller of Restrictive Business Practices and the Israeli court. To date, we have received approvals, subject to terms and conditions, from the Council, the Controller of Restrictive Business Practices and the Income Tax Commission. Subject to the final terms of the merger, further approval of the Income Tax Commission to the merger may be required. (See Item 4B. Information on the Company Business Overview - Arrangement for a Merger of Cable Television Operators).

Domestic Fixed Communications

On September 17, 2002, the Minister of Communications adopted the recommendations (subject to certain changes) of a committee formed by the Ministry for the establishment of policies and rules for the opening of competition in the field of domestic fixed communications, as the guiding policies in this field. The main purpose of the committee was to improve the benefits of the consumer in the field of domestic fixed communications, specifically by removing limitations for competition in this area. In accordance with the recommendations of the committee, among other things, the merger of the cable television operators and the entrance of the merged entity to the domestic telephony market, create opportunities for the opening of competition in the domestic fixed line telephony services market. For information regarding the provision of telephony services by the merged entity, see Item 4B. Information on the Company - Business Overview -Agreement for a Merger of the Cable Television Operators - Approval of the Controller of Restrictive Business Practices to the Merger - Interests in telephony services Regarding international telecommunication service providers (which include Barak I.TC. (1995) The General International Telecommunications Services Corp. Ltd.), the committee recommended, among other things, that the exclusivity period of these companies shall be extended until January 2004, subject to the condition that the international telecommunication rates shall not be increased during the extension period. In accordance with the Minister s decision, the Ministry shall act, during the extension period, such that international telecommunication services may be provided by new operators as of January 2004.

In order to implement the committee s recommendations, the Israeli parliament approved an amendment to the Telecommunications Law at the end of May 2003. Under the said amendment, as of September 1, 2004, the Minister may grant a special general license for domestic fixed telecommunications services without imposing on the holders of such licenses the obligation to provide their services to the entire public throughout the entire country or in any specifically defined area in Israel.

The adoption of the committee s recommendations may cause, among other things, the increase of competition in the telephony field of domestic fixed communications as of August 2004 and may increase competition in the international fixed line telephony services.

4B. Business Overview

We operate digital and analog cable television systems and provide a variety of channels and programs as one of three cable television operators in Israel. In addition we provide access to High Speed Internet over cable services. We believe that Israel is and will continue to be an attractive environment in which to provide cable television services for the following reasons:

Multi Channel Cable Television Market. As of December 31, 2002, there were approximately 1.84 million homes passed in Israel, with a penetration rate of approximately 58%. The high penetration rate for multi channel cable television services in Israel is attributable to the high penetration of televisions, multiple televisions and home video cassette recorders in homes, the fact that only three off-air channels in Hebrew are currently broadcast from Israel, and also to the demand for additional Hebrew language (including subtitled and dubbed) programs.

Growth in Subscriber Base. Between 2000 to 2002, the population of Israel grew at an average rate of approximately 2.3% per year.

Diverse Population. The cultural and linguistic diversity of Israel s population has created a large pool of potential cable television subscribers with different viewing needs. From 1991 through the end of 2002, approximately 895,000 new immigrants arrived in Israel, representing approximately 57% of the increase in Israel s population during that period. In addition, a substantial portion of Israel s population consists of first or second-generation immigrants, many of which we believe continue to speak the language of their country of origin and maintain strong cultural ties to that country.

Growth in the Number of Channels and Diversity of Content. We provide our subscribers with the most widely viewed cable television broadcasts in Israel. We continually aim to increase the number of channels we provide and improve the diversity of content, in accordance with the perceived requirements of our subscriber base. The following are the new channels that we provide since January 1, 2000, most of which are subtitled or dubbed in Hebrew or Russian, which we believe promotes viewer interest in cable television in Israel. The list is up to date as of May 31, 2003.

Since March 2000, the classical music channel (Mezzo);
Since February 2000, a new children s channel for preschoolers (Hop Channel);
Since June 2000, the American sport channel (ESPN) and the TV movie channel (Hallmark), the British entertainment channel (BBC Prime)
Since August 2000, the Cartoon Channel, the classic movie channel (TCM);
Since September 2000, the Russian classic movie channel (Nashe Kino);
Since November 2000, the action channel (AXN);
Since March 2001, the children s channel (Fox Kids), the Indian entertainment channel (Zee TV), the Romanian entertainment channel (Pro TV);
Since May 2001, the youth channel (BIP), and the 40 audio music channels;
Since July 2001, the European culture channel, (ARTE); the action channel, (Reality); the Arabic family, sport, children movie and music channels, (ART 1, 2, 3 4 and 5), the entertainment channel, (E!); the History Channel; the movie channels (Cinema 1, 2 and 3), the movie channel (MGM);
Since August 2001, the Adventure channel (Adventure 1);
Since September 2001, the lifestyle channel, (Good Life) and two extra home cinema digital channels;
Since November 2001, the telenovella channel (Viva Platina);
Since December 2001, the sports channels (Sport 5+) and (NBA);
Since January 2002, the general channel (Channel 10);
Since March 2002, the life style channel (Ego) the movie channel (Cinema Prime); and four music channels (MTV Base , MTV 2 , MTV Hits , and VH1 Classic);
Since April 2002, the Russian movie channel (MF);
Since June 2002, the IBA Arab channel (the Middle East Channel);
Since July 2002, the news channel (Fox News);
Since November 2002, the general Russian channel (Israel Plus) and the sports channel (Eurosportnews);
Since December 2002, the economics channel (CNBC), the sports channel (Fox Sport) and 4 regional radio channels;

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Since February 2003, the Russian channel (NTV Mir) and the sports channel (the Teams channel);
Since March 2003, the Russian History channel (History Russian); and
Since April 2003, the Judaism channel (Techelet).

We hold an option, exercisable in our discretion, to purchase 50% of an interactive youth application (named T.J.) that serves as a portal to our Youth Package , which we began to operate in November 2002.

Digital Broadcasting Services. In July 2001, we began to provide digital broadcasting services, as well as our analog broadcasting services. We offer our digital subscribers the digital Basic Package, and they may purchase all or part of any of the Premium Broadcastings.

For additional information see Item 4B: Products and Services-Basic Packages and Item 4B: Premium Broadcastings.

Pay-Per-View, Near Video on Demand. On September 14, 2000, we received a three-year permit, replacing a previous one, from the Ministry of Communications to provide Pay-Per-View and Near Video On Demand services, and in February 2001, a permit to provide Near Video on Demand services on the digital platform. These services are now governed by our Cable Broadcast Licenses. We have offered Pay-Per-View services since October 2000, which are commenced by digital and analog HeadEnd equipment and received at the subscriber s premises by analog and digital set-top boxes. We have not yet begun to offer Near Video On Demand Services.

Interactive Services. Since September 2001, we provide the following interactive services to our digital subscribers: Games Channels, Horoscopes, Weather and Classifieds. Since February 2002, we provide an entertainment programming guide service. Since November 2002, we operate an interactive youth application (T.J.) that serves as a portal to our Youth Package , which includes a multi-optional interactive screen. Interactive applications have been integrated into the Ego channel, since July 2002, and the Good Life channel, since August 2002. Since August 2002 we provide an interactive invoice service. Since December 2002, we provide our digital subscribers SMS and T-Mail messaging services through the use of the television screen and set-top box of the subscriber. Since December 2002, we began to implement an interactive voting application, which allows our subscribers to participate in television votes conducted on certain programs through the use of the subscriber set-top box. Since January 2003, we began to implement an interactive commercial application. Since February 2003, we began an interactive messaging service to subscribers, which allows us to send messages to subscribers regarding broadcasts and services in connection with broadcasts. During March 2003 and April 2003, as a result of the security situation in Israel at such time we provided an interactive portal to certain channels that include news and news updates, known as the Situation Room . Subject to the receipt of the relevant regulatory approvals, we intend to provide additional interactive services in the future, including the integration of interactive applications into additional channels, additional games channels, an interactive lottery and soccer lottery. We currently offer our digital subscribers Games Channels also on a pay-per-play basis (pay per game) or pay-per-use basis (pay per defined duration of time played), the use of which may be limited by the subscriber (for the purpose of parental control), on the basis of a predetermined maximum monthly fee.

Access to High Speed Internet Over Cable Services. On April 8, 2002, as part of our competitive activity in the telecommunications market, we began to provide access to High Speed Internet over cable services through our infrastructure, pursuant to our Telecommunications Infrastructure License.

Technologically Advanced Infrastructure. Due to the relatively recent buildout of the cable television industry in Israel, operators utilize advanced technologies, such as broadband, hybrid fiber optic/coaxial, or HFC, cable networks and digital video broadcasting, or DVB, platforms. The main benefits of using such technologies are the potential for greater capacity, increased functionality, improved broadcasting quality, and development of two-way communication based services. We installed and utilize a DVB platform, and previously upgraded our HFC network into a full two-way expanded bandwidth plant. We successfully employ an access to High Speed Internet over cable platform. Based on our infrastructure, we plan to gradually implement more service layers, such as video on demand and personal video recorder (or PVR) services, enhanced television interactive applications and other services (which utilize the cable television platform upon other alternative platforms).

Integrated Fiber-Optic Network. The broadband networks of the three cable television operators in Israel are connected through nationwide fiber optic cable links. This interconnection among the cable television operators creates an opportunity, subject to regulatory approvals, to develop and provide subscribers throughout Israel with services such as telecommunications using the already installed cable television networks.

Services to the Business Sector. We are currently preparing for the commencement of the provision of additional communication services designated to businesses, including Internet Protocol Visual Private Network (or IP VPN) and symmetrical broadband services for the business sector.

Strategy

Our mission is to leverage our cable television infrastructure and market share to be a leader in the Israeli information, telecommunications and entertainment industry. In order to achieve our mission, we are implementing strategies designed to:

- increase our value-added services offerings to our subscribers;
- expand into other telecommunications activities;
- enter into mergers, acquisitions and strategic alliances to add to our offering and expand our market share.

Competitive Strengths

We believe that the following competitive strengths differentiate us from our competitors and will assist us in achieving our mission and implementing our strategies:

state-of-the-art technology and an advanced network and infrastructure which we own entirely including two-way broadband transmission, HFC cables, and a fully digitalized broadcasting system.

a diversified and rich selection of programming content;

high quality of broadcasting service and support for customers;

as of December 31, 2002, a large customer base which contains approximately 275,000 subscribers, constituting a penetration rate of approximately 60% in our license areas;

a highly experienced and dedicated management team and staff;

built in technological unique advantages, such as wide bandwidth, 2-way communication, one pipe for various, multiple services, segmented network (which allows reuse of bandwidth and implementation of narrowcast and Unicast services); and

reasonable fees for our cable television broadcast offerings and access to High Speed Internet over cable services, and for other services.

Availability and Sources of Programming

The increasing availability of cable television in Israel has provided an attractive alternative to the limited off-air television programming and the use of video cassette recorders and DVDs. We offer our analog and digital subscribers a single tier of certain channels (within the framework of the analog and digital basic broadcast packages, known as the Basic Packages), and we offer our digital subscribers the possibility for additional channels and packages in their license areas (within the framework of our Premium Broadcastings). For information regarding the channels and packages included in the Basic Packages and the Premium Broadcastings, see Item 4B: Products and Services - Basic Packages and Item 4B: Products and Services - Premium Broadcastings . A significant amount of the most popular channels available to cable television operators in Israel is provided by I.C.P. and by independent producers. The three cable television operators in Israel currently provide the same program scheduling on most of the channels in each of their license areas, enabling subscribers throughout Israel to watch the same program at the same time.

We aim to diversify and improve the content quality we provide to our subscribers. We do so by adding new broadcasting channels and enriching the existing ones. For example, we provide subscribers with broadcasts of the English football Premier League, the U.S. National Basketball Association League, the European Football Association Champion League, the French Open and films and popular series from leading major studios around the world. In addition, we offer our subscribers new interactive applications.

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Products and Services

Overview of our Cable Television Services

We offer cable television analog and digital subscribers a single tier of basic service (within the framework of the analog and digital Basic Packages). We offer our digital subscribers the possibility for additional channels and packages (within the framework of our Premium Broadcastings) and services. Similar services to those we offer our digital subscribers are also offered by YES.

Subscribers are offered access to a variety of Hebrew language programming (including original, subtitled and dubbed), a home shopping channel, off-air channels originating in Israel and other selected countries, and satellite television channels. We charge subscribers an initial installation fee of approximately NIS 85 plus VAT, and a monthly subscription fee for the analog and the digital Basic Packages of approximately NIS 144 plus VAT. We also require a deposit of approximately NIS 84 plus VAT, for the regular analog set-top box (for those subscribers without cable-ready televisions), or NIS 169 plus VAT, for the addressable analog set-top box, and a deposit of approximately NIS 254 plus VAT, for the digital set top box. We partially refund the deposit when the set-top box is returned. The refund amount (which is linked to the Israeli consumer price index) is reduced to reflect 10% annual depreciation for each year or portion of a year in which the subscriber used the set-top box. In accordance with an amendment to regulations promulgated under the Telecommunications Law approved by the Economic Committee of the Israeli parliament on June 16, 2003, the deduction from the deposit for the set-top box shall be 10% of the value of the set-top box. Alternatively, our subscribers may elect to lease the set-top box for a monthly fee that ranges between NIS 10 and NIS 15 including VAT.

We also charge subscribers fees for reconnection, installation of additional outlets in subscribers households; and provision of cable television services on the additional outlets. These fees are all subject to value added tax at a rate of 18%.

Programming

We currently transmit programming on varying numbers of channels in our operating areas, which consists of off-air channels, satellite channels, dedicated channels, and other channels, all as more fully detailed below, including in the tables of the analog and digital Basic Packages and in the table which sets forth those additional channels and packages that are included within the Premium Broadcastings which we provide to digital subscribers in the tiering system. For discussion of our risks related to programming, see Item 3. Risk Factors , and for a discussion of certain of our costs associated with programming, see Item 5. Operating Financial Review and Prospects Operating Expenses .

Off-Air Channels. The off-air channels we transmit to our subscribers include the Israel Broadcast Authority channels (Channels 1 and 33), the Middle East Channel, the commercial channels (Channels 2 and 10), the general Russian Channel, as well as other off-air channels, which broadcast from other selected countries. Although subscribers can receive transmission of these off-air channels through a household antenna or a satellite dish, the antennae located on our HeadEnds enable subscribers to obtain superior picture and sound quality.

We are not required to pay royalties with respect to off-air channel broadcasts. We and the other cable television operators have agreed, however, to pay royalties to certain organizations representing Israeli performing artists with respect to copyrighted materials broadcasted by the cable television operators. For the years ended December 31, 2000, 2001 and 2002, we paid royalties to such organizations of approximately NIS 2.8 million, NIS 2.8 million, and NIS 3.0 million, respectively.

Satellite Channels. We transmit to our subscribers broadcasts of foreign and Israeli television channels which we receive at our HeadEnds via satellite. We pay fees for the right to transmit certain of these broadcasts. The portion of these fees for which we are responsible is based on the number of our subscribers in a given payment period. We have not received permission to transmit the respective broadcasts from all foreign satellite television operators whose broadcasts we transmit. However, pursuant to our Licenses, and subject to the permission of the Council, our freedom to remove channels from the Basic Packages is limited. The broadcasting regulations, as amended, prohibit the broadcasting of channels or programs without the consent of the original broadcaster. Furthermore, there can be no assurance that the satellite television operators to whom we do not currently make payments will not request payments from us in the future. In addition, a lawsuit was filed against us in connection with these matters. See Item 8A. Consolidated Statements and Other Financial Information - Legal and Arbitration Proceedings .

Other Channels: We broadcast a wide variety of additional channels, including those channels listed in the Basic Packages tables below, and those pursuant to our tiering, Pay-Per-View and interactive services.

On May 30, 2001 we commenced broadcasting of the adult content channels. From October 2001, pursuant to amendments to the Telecommunications Law and Council decisions, we transmitted adult content channels by way of Pay-Per-View only. Pursuant to further amendments to the Telecommunications Law, broadcasts that include abominable material in the meaning of the Israeli Penal Law, 1977, and which include certain content as set forth in the Telecommunications Law, is prohibited as of August 2002. Following such further amendment, we ceased to transmit adult content channels also by way of Pay-Per-View. On June 12, 2003, the Council resolved to approve the broadcast of the Playboy channel, subject to certain conditions and limitations, under which, among other things, the Playboy channel will be transmitted only at certain stipulated times and offered to digital subscribers as a separate pay channel and not as part of the digital Basic Package. We have commenced broadcasts of the Playboy channel pursuant to and in accordance with the conditions and limitations set forth in the Council s latter decision. Such conditions and limitations stipulate that, among other things, the Playboy channel will be transmitted only at certain stipulated times and offered to digital subscribers as a separate pay channel and not as part of the digital Basic Package; Cable Broadcast Licensees are required to take reasonable measures to ensure that the channel shall be purchased only by subscribers over the age of 18; the channel will be coded such that access will be available only by a personal code; and Cable Broadcast Licensees are required to transmit during the transmission of the channel certain broadcasts regarding the prohibition on exposure of children and youth to the channel. For information regarding a petition filed in the Israeli Supreme Court of Justice by the producers of the Playboy channel, see Item 8A: Consolidated Statements and Other Financial Information - Legal and Arbitration Proceedings .

Locally Produced Programming. In 1989, together with the other Israeli cable television operators, we established a company named ICP Israel Cable Television Programming Company Ltd., for the purpose of jointly purchasing and producing content for our local channels. Today, ICP creates, produces and acquires content for two channels (family and movies). We have approximately 25% ownership interest in ICP and make payments to it based on the number of our subscribers. For the years ended December 31, 2000, 2001 and 2002, we paid ICP approximately NIS 60.7 million, NIS 71.0 million and NIS 62.9 million, respectively.

Under the Telecommunications Law, we are required to allocate between 8% and 12% of our annual income derived from subscriber fees to production or purchase of original locally produced broadcasts, and the Council has the authority to fix the percentage from the 8%-12% range, while taking into account the economic status of the cable television operators in the field of cable broadcasts. For information regarding the Council s decisions in connection with this matter, see Item 4B. Information on the Company Business Overview - The Telecommunications Law and Our Licenses - Specific Terms and Conditions of our Cable Broadcast Licenses - Broadcasts and Programming .

Under the Telecommunications Law, we are required to provide up to one-sixth of our network capacity for broadcasting, to holders of special cable television licenses for specific channels. In addition, we have allocated programming time to broadcasting by local community organizations and the public educational channel, which we are obliged to broadcast according to the Telecommunications Law. With the exception of the broadcasts by local community organizations and the public educational channel, all such special cable television licensees are required to pay for the use of our network capacity. In the event that a merger between the Israeli cable television operators is consummated, we shall be under an obligation to allow other broadcast license holders to have access to our network infrastructure, within three months from the date so requested by the other licensee or producer. According to the approval of the Controller for Restrictive Business Practices to the proposed merger, if we are unable to reach a commercial agreement with such broadcast licensee or producer within 60 days, the matter must be referred to arbitration and the arbitrator must act in accordance with the instructions of the Controller of Restrictive Business Practices.

Local News Broadcasts. Our licenses also require that we provide periodic local news broadcasts in each license area. The content of our local news and local community programs varies in our operating areas. In accordance with the Council s decisions of December 2002 and February 2003, a Cable Broadcasting Licensee may produce local news broadcast for seven license areas through an external producer, subject to the Council s approval. Accordingly, we and the other two Israeli cable television operators entered into an agreement dated January 5, 2003, as amended on March 5, 2003, with Today s Cable News the Local News Company Ltd., commonly referred to as JCS , whereby JCS shall produce local news for the cable television operators for their respective areas in consideration of NIS 42.48 million per annum (linked to the Israeli consumer price index and subject to adjustments). The payment of the consideration will be divided between the 3 cable television operators, in proportion to the number of their respective subscribers. Of this consideration, we are required to pay NIS 11 million. Under the agreement, the cable television operators undertook, among other things, to provide JCS exclusive use of a production studio for the production of the local news in consideration of approximately NIS 12.3 million per annum (linked to the Israeli consumer price index plus VAT). The consideration received for use of the production studio will be divided between the 3 cable television operators, in proportion to the number of their respective subscribers. Of this consideration, we will be entitled to approximately NIS 3.2 million. The agreement is for an initial period of 5 years, and may be extended by the cable television operators for additional periods. The agreement with JCS was approved by the Council on March 6, 2003. The effectiveness of the agreement with JCS is subject to the approval of the Controller for Restrictive Business Practices, to the extent such approval is required, and on February 20, 2003, the parties requested the approval of the Controller. To date, the approval of the Controller to the JCS agreement has not been received.

Commercial Advertising and Dedicated Channels. According to the Telecommunications Law, the Council may grant special licenses to independent producers of specific dedicated cable television channels, and such channels may be entitled to offer commercial advertising. The Economic Committee of the Knesset decided on January 27, 1998, that such dedicated channels will be: an Arabic channel, a Jewish traditional channel, two news channels, an Israeli music channel and one channel or more in foreign languages for new immigrants arriving to Israel. In 2001 and 2002, the Council selected winning bids for the tender for a News Channel, a general Russian channel and an Israeli music channel, all of which will be permitted to broadcast commercials. The general Russian Channel commenced broadcasts as of November 2002. As yet, the News Channel and the Israeli music channel have not commenced broadcasts.

Currently Channel 2, Channel 10 and the general Russian Channel are the only locally produced channels (which have commenced broadcasting) that have permits to air commercials. Some foreign satellite channels also air commercials. Permits have also been granted to special broadcast licensees as described above, namely the News Channel and the Israeli music channel, which have not commenced broadcasts to date. In addition to the prohibition on broadcasting commercials on our local channels, the Telecommunications Law, as amended, prohibits the broadcasting of commercials on channels that the Council has decided are targeted mainly to the Israeli public, without the prior approval of the Council. The Council has set certain criteria regarding these stipulations.

The approval of the Controller of Restrictive Business Practices to the merger of the Israeli cable television operators provides, among other things, that if the merged broadcasting entity receives approval to air advertisements on its channels, then the Controller shall have the power to impose additional restrictions upon the entity. We have no assurance that the merged entity shall receive any such approval.

Basic Packages

In accordance with our Broadcasting License, we must provide each of our subscribers (analog and digital) basic broadcasts that shall include:

Israel s channels 1 and 33 and the Middle East Channel, of the Israeli Broadcasting Authority;

the commercial channels (Channel 2 & 10);

the Israeli educational channel;

dedicated channels pursuant to the Telecommunications Law (which currently only include the Shopping and Russian Channels, but may in the future also include the News and Music Channels that have won tenders, and other channels that have yet to be tendered);

regional news and community broadcastings;

channels of special cable broadcast licensees according to the Council s instructions, on the digital service only (none of which exist to date); and

the EPG service, on the digital service only.

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Our Cable Broadcast Licenses stipulate that, in the event that we wish to reduce the scope of the basic broadcasts, we must request the Council s approval. In the event that the scope of the analog basic broadcasts has been reduced, the Council may instruct us (subject to the approval of the Minister) to reduce the price for such reduced package to an amount determined by the Council. In such case, we would be entitled to present our position to the Council prior to it rendering its decision.

Our Cable Broadcast Licenses stipulate that we may not charge our analog subscribers for the basic broadcasts more than approximately NIS 148 plus VAT, in the Holon/Bat Yam and Haifa/Hadera regions, approximately NIS 140 plus VAT, in the Sea of Galilee/Netanya region, and approximately NIS 141 plus VAT, in the Golan/Sefat and Kiryat Shemoneh region. Additionally, we may not charge our analog subscribers for a movie provided on Pay-Per-View basis more than approximately NIS 15 plus VAT, per broadcast. Such fees may be linked to the Israeli consumer price index from February 2002. Our Cable Broadcast Licenses do not stipulate fees for digital subscribers. Under regulations promulgated pursuant to the Telecommunications Law, we may determine our subscriber fees for digital subscribers (including the basic broadcasts package). Such fees that we set for our digital subscribers must be reasonable, and the Minister may direct us to amend such fees if he finds, among other things, that they are harmful to competition, discriminatory or misleading. The Council s approval to the proposed merger of the Israeli cable television operators stipulates, as a condition to the merger, that we, or the merged entity, will be subject to a maximum subscriber fee for both the digital and analog basic broadcasts packages of NIS 156 incl. VAT, linked to the combined index, that includes the Israeli consumer price index of December 2001 (published January 15, 2002) and the US dollar exchange rate as published by the Bank of Israel, or any other index as shall be determined in regulations. The effectiveness of the Council s approval regarding the said linkage to the combined index is subject to the amendment of the applicable regulations promulgated under the Telecommunications Law. To date, the Ministry has not adopted such an amendment.

The Council has determined that all channels in the Basic Package on our digital platform must be included in the Basic Package on our analog platform, unless otherwise authorized by the Council.

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Digital Basic Package

The following table lists information regarding the Basic Package that we offer to our digital subscribers as of May 31, 2003.

Channel	**Description**	**Language**[(1)]
Mosaic	Split-screen showing all channels	
Channel 3	Entertainment	Hebrew
Movies	Cinema Movies	Hebrew
Sport	Local and intentional games & Competition	Hebrew
Children	Cartoons, movies & other children entertainment	Hebrew
MTV	Europe video music	English
Channel 8	Culture, Science & Education	Hebrew & Russian

Channel 9	Local news & others-general	Hebrew
Israel 10	Third national channel	Hebrew
Israel 1	First national channel	Hebrew
Israel 33	Israeli parliament channel	Hebrew
CNN	World news	English
Sky news	World news	English
BBC World	Collection of BBC best programs	English
ORT- Russia	Russian channel	Russian
RTR Russia	Russian channel	Russian
NASHA KINO	Russian Channel	Russian
RTV Int	Russian Channel	Russian
NTV MIR	Russian Channel	Russian
National Geographic	Localized channel of NGC	Hebrew
Star World	Entertainment	English
Shopping	Israeli shopping channel	Hebrew
Israel 2	Second national channel	Hebrew
Education	Israeli educational channel	Hebrew
SAT 3	German channel	German
RTL	German channel	German
TV5	French channel	French
France 2	French channel	French
Arte	Culture	French
Euro sport	European sport broadcasting	English
VH-1	Video Music	English
TVE	Spanish channel	Spanish
RETE 4	Italian channel	Italian
TRT 1	Turkey 1	Turkish
TRT 2	Turkey 2	Turkish
INTERSTAR	Turkish channel	Turkish
DUNA TV	Hungarian channel	Hungarian
Emergency (2)	Emergency communications	Hebrew
SAT 1	German channel	German
LBC	Arabic channel	Arabic
Viva	Teledrama Channel	Hebrew
Fashion TV	Fashion TV	French
MEZZO	Classic Music Channel	French
Hop	Children Channel	Hebrew
Hallmark	Series and Movies	Hebrew/Russian
BBC Prime	English channel	English/ Hebrew
AXN	Action	Hebrew
TCM	Movies	English/ Hebrew
ESPN	Sport	English
CARTOON	Cartoons, movies & other Children entertainment	English
TV 7 -TUNIS	Tunisian channel	Arabic
Jordan Arabic	Jordanian channel	Arabic
Morocco	Moroccan national channel	Arabic
Egypt	Egyptian national channel	Arabic
METV	Free Lebanon television	Arabic/English
MBC	Arabic channel	Arabic
Almustakble	Entertainment	Arabic
Saudia	National	Arabic

Channel	**Description**	**Language**(1)
Syria	National	Arabic
Aljazeera	News	Arabic
Dubai	National	Arabic
Middle East Channel	General	Arabic

EPG	User Guide	Hebrew/English /Russian
User Guidance Channel	User Guidance Channel	Hebrew /Russian
13 Radio Channels	Music, News General	Hebrew /Russian

(1) Originated, subtitled or dubbed, as indicated.

(2) Operates only during emergencies.

Analog Basic Package

The following table lists information regarding the Basic Package that we offer to our analog subscribers as of May 31, 2003.

Channel	**Description**	**Language(1)**	*Bat-Yam/ Holon*	*Haifa*	*Netanya/ Hadera*	*Golan*	*Arab section*	*Galilee*
Mosaic	Split-screen showing all channels		ü	ü	ü	ü	ü	ü
Channel 3	Entertainment	Hebrew	ü	ü	ü	ü	ü	ü
Movies	Cinema Movies	Hebrew	ü	ü	ü	ü	ü	ü
Sport	Local and intentional games & Competition	Hebrew	ü	ü	ü	ü	ü	ü
Children	Cartoons, movies & other Children entertainment	Hebrew	ü	ü	ü	ü	ü	ü
MTV	Europe video music	English	ü	ü	ü	ü	ü	ü
Channel 8	Culture, Science & Education	Hebrew/ Russian	ü	ü	ü	ü	ü	ü
Local channel	Local news & others	Hebrew	ü	ü	ü	ü	ü	ü
TVE	Spanish channel	Spanish	ü	ü	ü	ü	ü	ü
Israel 10	Third national channel	Hebrew	ü	ü	ü	ü	ü	ü
Israel 1	First national channel	Hebrew	ü	ü	ü	ü	ü	ü
CNN	World news	English	ü	ü	ü	ü	ü	ü
Sky news	World news	English	ü	ü	ü	ü	ü	ü
ORT- Russia	Russian channel	Russian	ü	ü	ü	ü	ü	ü
RTR Russia	Russian channel	Russian	ü	ü	ü	ü		ü
National Geographic	Localized channel of NGC	Hebrew	ü	ü	ü	ü	ü	ü
Star World	Entertainment	English	ü	ü	ü	ü		ü
RETE 4	Italian channel	Italian	ü	ü	ü	ü	ü	ü
Shopping	Israeli shopping channel	Hebrew	ü	ü	ü	ü	ü	ü
Israel 2	Second national channel	Hebrew	ü	ü	ü	ü	ü	ü
Education	Israeli educational channel	Hebrew	ü	ü	ü	ü	ü	ü
SAT 3	German channel	German		ü		ü	ü	ü
RTL	German channel	German	ü	ü	ü			ü
Jordan Arabic	Jordanian channel	Arabic	ü	ü	ü	ü		ü
TV Guide	TV broadcasting programs	Hebrew	ü	ü	ü	ü		
Morocco	Moroccan national channel	Arabic	ü	ü	ü	ü	ü	ü
Egypt	Egyptian national channel	Arabic	ü	ü	ü	ü	ü	ü
METV	Free Lebanon television	Arabic/ English	ü	ü	ü	ü	ü	ü
MBC	Arabic channel	Arabic	ü	ü	ü	ü	ü	ü
Israel 33	Israeli parliament channel	Hebrew	ü	ü	ü	ü	ü	ü
TV5	French channel	French	ü	ü	ü			ü
France 2	French channel	French	ü	ü	ü	ü		ü
Euro sport	European sport broadcasting	English	ü	ü	ü		ü	ü
VH-1	Video Music	English	ü	ü	ü	ü	ü	ü
TRT1	Turkey 1	Turkish	ü		ü			
TRT2	Turkey 2	Turkish	ü					
DUNA TV	Hungarian channel	Hungarian	ü	ü	ü	ü		ü
INTERSTAR	Turkish channel	Turkish	ü	ü	ü	ü	ü	ü

Emergency (2)	Emergency communications	Hebrew						
TV 7 -TUNIS	Tunisian channel	Arabic		ü	ü		ü	
SAT 1	German channel	German	ü	ü	ü	ü	ü	ü

Channel	**Description**	**Language**[(1)]	*Bat-Yam/ Holon*	*Haifa*	*Netanya/ Hadera*	*Golan*	*Arab section*	*Galilee*
LBC	Arabic channel	Arabic		ü		ü	ü	
Viva	Teledrama Channel	English / Hebrew	ü	ü	ü	ü	ü	ü
Fashion TV	Fashion TV	French	ü	ü	ü	ü		ü
MEZZO	Classic Music Channel	French	ü	ü	ü	ü	ü	ü
Hop	Children Channel	Hebrew	ü	ü	ü	ü	ü	ü
RTV Int.	Russian Channel	Russian	ü	ü	ü	ü		ü
Hallmark	Series and Movies	English/ Hebrew	ü	ü	ü	ü	ü	ü
BBC Prime	English channel	English/ Hebrew	ü	ü	ü	ü	ü	ü
AXN	Action	English/ Hebrew	ü	ü	ü	ü	ü	ü
TCM	Movies	English/ Hebrew	ü	ü	ü	ü	ü	ü
ESPN	Action	English	ü	ü	ü	ü	ü	ü
CARTOON	Cartoons, movies & other Children entertainment	English	ü	ü	ü	ü	ü	ü
NASHA KINO	Russian Channel	Russian	ü	ü	ü	ü	ü	ü
Almustakble	Entertainment	Arabic					ü	
Saudi	National	Arabic					ü	
ART 1	Family	Arabic					ü	
ART 2	Sport	Arabic					ü	
ART 3	Children	Arabic					ü	
ART 4	Movies	Arabic					ü	
ART 5	Music	Arabic					ü	
Syria	National	Arabic					ü	
Aljazeera	News	Arabic					ü	
Dubai	National	Arabic					ü	

(1) Originated, subtitled or dubbed as indicated.

(2) Operates only during emergencies.

Tiering

On April 5, 2001, the Council published its decision concerning its policy in relation to broadcasting in the tiering system. The tiering system enables us to supply to our digital customers the digital Basic Package at a fixed price and additional single channels and packages of channels for additional payment. The policy behind the Council s decision is that the tiering system should enable customers to receive and pay for only the channels or packages chosen by them. The Council will not oblige us to offer our broadcastings in the tiering system in the analog transmission platform. We received approval from the Council to provide digital broadcast services in a tiering system on May 10, 2001. We are allowed to operate the tiering system only in our digital transmission platform. Marketing of our tiering broadcasting packages began in July 2001.

The Council s decision that permits tiering in our digital transmission platform is subject to our fulfilling a commitment that we made to the Ministry of Communications on January 7, 2001, to supply and connect digital set-top boxes to our customers over the years 2001 to 2004. For additional information, see Item 4A. Information on the Company - History and Development of the Company - Important Events in the development of Cable Television and telecommunication industry, and our business - Digital Broadcasting .

As of December 2002, we and the other two Israeli cable television operators offer unified tiering packages, in the framework of which we changed the structure of the tiering packages we offer to our digital subscribers and the channels included in such packages. For a list of our channels and packages and the combinations of packages we offer as part of our tiering system, see Item 4B. Item 4B: Products and Services - Premium Broadcastings.

Premium Broadcastings

Pursuant to the Council s approval dated May 10, 2001, we may supply in our digital broadcastings those Premium Broadcastings that the Council has approved. As of May 31, 2003, approximately 56% of our subscribers are subscribers to the digital broadcasting system and of those, 86% are provided with packages or channels through the tiering system.

Premium Broadcastings may be provided only to a digital subscriber that has purchased the digital Basic Package. The purchase of any of the Premium Broadcastings may not be conditioned upon the purchase of other Premium Broadcastings. Rather, digital subscribers may purchase all or any part of the Premium Broadcastings in any combination of channels and packages, as they deem proper.

The following channels and packages have been approved by the Council to be included within the Premium Broadcastings in the tiering system as of June 2003.

Name of Package	Channels Included
Movies	Cinema 1,2,3 Cinema Prime/COOL MGM
Entertainment	Bip E! History Channel Adventure 1 Life Style Viva Platina Leisure Guide Ego
Men & Sports	Channel 5+ NBA Ego Reality TV Adventure 1 Teams channel Eurosportnews Fox Sport CNBC
MTV	MTV HITS MTV2 MTV BASE VH1 CLASSIC
Russian	Cinema 1,2 & 3 Cinema Prime/COOL Mega Film History (Russian) Reality TV
Games	Gogo Klick Gogo Gold

Music Choice	40 Audio Channels
Various channels a la carte	Zee TV ART 1-5 Pro TV Techelet Playboy
Communication	T-mail & SMS
Children s	Cinema COOL Fox Kids Game channel
Youth	BIP MTV HITS MTV2 MTV BASE VH1 CLASSIC Leisure Guide Game channel
Interactive services	Weather Classifieds Horoscope

We offer combinations of packages as part of our tiering system as follows:

***Duet*:** Any combination of two of the following channels and packages: Cinema 1, 2 & 3 ; Children ; Youth and Entertainment .

***Duet Plus*:** Any combination of two of the following channels and packages: Movies ; Children ; Youth ; Entertainment ; Men & Sports and Russian .

Trio: Any combination of three of the following packages and channels: Cinema 1, 2 & 3 ; Children ; Youth ; Entertainment and Russian .

Trio Plus: Any combination of three of the following packages and channels: Movies ; Children ; Youth ; Entertainment ; Men & Sports and Russian

4U: Any combination of four packages.

Take 5: Any combination of five packages.

We provide our digital subscribers interactive services of Weather, Classifieds and Horoscopes, for no additional consideration.

Shopping Channel

In late 1995, we began transmitting a home-shopping channel, which offers products directly to cable television subscribers, known as the Shopping Channel . The Shopping Channel is broadcast pursuant to a special broadcast license and is provided to our subscribers as part of the digital and analog Basic Packages. Through 2003, we are entitled to a fee from the producer of the Shopping Channel for the use of one of our channels. For the years ended December 31, 2000, 2001 and 2002, we have received approximately NIS 2.1 million, NIS 2.1 million and NIS 1.2 million, respectively, from the Shopping Channel in fees.

In addition, on January 2, 2003, the Council determined its policy regarding shopping channel broadcasts by a cable broadcast licensee following the receipt of a separate approval from the Council for the broadcasts of shopping channels. To date, we have not requested permission to broadcast additional shopping channels.

Pay-Per-View and Near Video On Demand

Pay-Per-View and Near Video On Demand services are covered by our Cable Broadcast Licenses. We are subject to maximum price restrictions for analog Pay-Per-View services, of approximately NIS 15 plus VAT, per broadcast. We are also subject to restrictions regarding payment for specific broadcasts, the time duration of a single broadcast and certain restrictions regarding the cancellation of a Pay-Per-View order by a subscriber. We are authorized to offer live broadcasting by Pay-Per-View. We began providing Pay-Per-View services to our subscribers in October 2000. We currently broadcast 4 Pay-Per-View channels on the analog platform and 6 on the digital platform. In the past we offered adult content by way of Pay-Per-View, subject to certain regulated restrictions, however following amendments to the Telecommunications Law, effective as of August 2002, we ceased to broadcast adult content by way of Pay-Per-View. Following the Council s decision of June 16, 2003, we have commenced broadcasts of the Playboy channel on a la carte basis, in accordance with the conditions and limitations set forth in the said decision. We have not yet begun to offer Near Video On Demand services to our subscribers.

Internet Services

Pursuant to our Telecommunications Infrastructure License, on April 8, 2002, we launched a service of access to High Speed Internet over cable. Initially we offered promotional packages to the subscribers to the trial services and other initial subscribers to the service. We currently offer access to High Speed Internet over cable services in all of our License areas, and at December 31 2002, we had 21,849 access to High Speed Internet over cable subscribers. The table below sets forth the products we offer under our access to High Speed Internet over cable services.

Name of Product	***Upload Speed***	***Download Speed***
Winner Start	64Kbps	0.15Mbps
Winner First	64Kbps	0.256Mbps
Winner	96Kbps	0.75Mbps
Winner Plus	128Kbps	1.5Mbps
Winner Premium	150Kbps	3Mbps

In addition, we offer our Internet subscribers the option to upgrade the Upload Speed of our access to High Speed Internet over cable products, by 64Kbps (Extra) and 128Kbps (Extra Plus).

Our access to High Speed Internet over cable service allows the user to directly access the Internet over cable broadband infrastructure, through the use of a cable modem and personal computer, and there is no need for dial up activity. We recently began to provide Internet services to certain establishments, businesses and communal settlements in Israel. We have upgraded our infrastructure to prepare for the provision of data over cable services in the future. The technology upgrade is compliant with the technologies of the other parties to the proposed merger of the Israeli cable television operators. In the event that the proposed merger is consummated it will allow and support the merged entity s ability to provide these services throughout the license areas of the merged entities. By May 31, 2003, we have purchased approximately 43,000 cable modems and intend to purchase more in the future in accordance with the market penetration of the service.

Interactive Services

As at May 2003, we supply our digital subscribers with interactive services, including Games Channels, Horoscopes, Weather and Classifieds, an entertainment programming guide service, an interactive youth application (T.J.) that serves as a portal to our Youth Package , interactive applications integrated into the Ego channel and the Good Life channel, an interactive invoice service, messaging services (T-mail and SMS), interactive voting applications, interactive commercial applications and an interactive messaging service to subscribers (which allows us to send messages to subscribers regarding broadcasts and services in connection with broadcasts). During March 2003 and April 2003, as a result of the security situation in Israel at such time, we provided an interactive portal to certain channels that include news and news updates, known as the Situation Room . We intend, subject to the receipt of the relevant regulatory approvals, to provide additional interactive services in the future, including the integration of interactive applications into additional channels, additional games channels, an interactive lottery and soccer lottery. We currently offer our digital subscribers Games Channels also on a pay-per-play basis (pay per game) or pay per-use basis (pay per defined duration of time played), the use of which may be limited by the subscriber (for the purpose of parental control), on the basis of a predetermined maximum monthly fee.

In March 2001, we entered into an agreement with Connect TV Ltd., which was subsequently replaced by a memorandum of understanding dated December 25, 2002. Under these agreements, Connect TV agreed to supply us with certain games and other services for our interactive television activity. Until January 2003, Dankner Investments Ltd., our controlling shareholder, held approximately 31% of the issued share capital of Connect TV, at which time Dankner Investments Ltd. sold all of its shareholdings in Connect TV. For the years ended December 31, 2001 and 2002, we have paid Connect TV approximately NIS 2.8 million and NIS 1.2 million, respectively, for services rendered.

In October 2001, we received a special license to conduct a technological trial to provide messaging services to our digital subscribers, such as T-Mail and SMS, on our cable network, under which we provided T-Mail and SMS services through the use of the television screen and set-top box of the subscriber on a trial basis. In August 2002, the Ministry granted us special licenses to provide such services, which shall expire in July 2003. Under these special licenses, as subsequently amended in October 2002, we may provide SMS services (between our subscribers and subscribers of mobile cellular telephone service providers) and T-Mail services (from television to television, between our subscribers and between our subscribers and subscribers of Internet service providers). To date, we provide these messaging services on a commercial basis to approximately 1,000 subscribers. In connection with the messaging services we provide, including, among other things, T-Mail and SMS, we entered into a memorandum of understanding with Comverse Network Systems Ltd. in July 2001, regarding the supply by Comverse of products for interactive television unified messaging using Comverse s TVGATE system.

In 2002 and 2003, we entered into agreements with Cellcom Israel Ltd., Partner Communications Company Ltd. and Pelephone Communications Ltd., regarding SMS messaging between our cable network and the cellular mobile networks of the said entities by our subscribers and the subscribers of such entities.

Set- top boxes

While our broadband network is configured to support a wide variety of services, such as Pay-Per-View, Premium Broadcastings and Interactive Services, it is necessary to provide addressable set-top boxes to subscribers in order to implement such services. We bear the cost of the addressable set-top boxes supplied to subscribers having set-top boxes in their homes. Those subscribers that are provided with addressable set-up boxes shall bear, in whole or in part, the cost of the set-top boxes by way of a deposit. We must not charge a fee for the deposit of the set-top box equal to more than the value of the set-top box at the time of the deposit. In accordance with the terms of our Cable Broadcast Licenses, as amended by the Council on March 6, 2003, our subscribers may alternatively elect to lease the set-top box for a monthly fee. We must not charge an aggregate fee for the lease of the set-top box equal to more than the value of the set-top box. On June 16, 2003, the Economic Committee of the Israeli parliament resolved to approve an amendment to regulations promulgated under the Telecommunications Law, which regulates the ability of the Cable Broadcast Licensees to lease the set-top box to the subscriber, at the subscribers choice, in accordance with the terms of the Cable Broadcast License, and in addition, pursuant to this amendment Cable Broadcast Licensees are also allowed to sell the set-top box to subscribers, at the subscribers choice, in consideration of an amount that shall not be more than the value of the set-top box.

Sales, Marketing and Customer Service

Sales and Marketing. Our marketing strategy is to increase the subscriber penetration within our License areas and maintain subscriber satisfaction in order to preserve low subscriber churn rate and to increase the average revenue per user (ARPU). We market and sell our services through the combined efforts of integrated sales, marketing, technical and customer service groups. We train our personnel to provide information concerning technological advances and to address the specific requirements of potential and existing subscribers. We monitor the performance of these personnel through a variety of supervising methods. In addition, we participate in rating surveys conducted by independent organizations, including I.C.P. We also use training programs and surveys prepared by independent professional marketing consultants to help increase the effectiveness and efficiency of our sales and marketing groups.

During the initial phase of the buildout of our network, we sought to create awareness of our cable television services and stimulate subscriber demand. In an effort to increase subscriber penetration, we initially relied on door-to-door visits by sales personnel who introduced our products and services by offering on-location demonstrations. We also utilized billboards, direct mail and mass marketing programs, including radio advertising, print media and shopping mall demonstrations, to further marketing efforts. As the buildout of the cable television network continued and subscriber penetration rates increased in the License areas, we placed greater emphasis on telemarketing and direct mail efforts to target those groups that had not subscribed for our services, tailoring the campaign to the specific requirements of such subscribers. This targeted marketing had the effect of reducing the marketing costs incurred in attracting new subscribers. We have further refined our focus to preserve our existing customer base and, in this context, we have established marketing locations in centrally located consumer malls within our license areas.

As part of our effort to attract and maintain subscribers, we market our services by advertising particular programs that are broadcast on various channels on our cable network which we believe would be of interest to potential subscribers on the off-air Channels 2 (including interactive advertisements) and 10 and the general Russian Channel, and through print media, direct mail, telemarketing and cross-promotions on dedicated channels. In addition, as part of our effort to maintain subscribers, we promote channels and programs that we broadcast on channels that we broadcast. We also invest in promotions specifically aimed at the Russian sector in Israel due to the potential of this market. As of the end of April 2002, in accordance with the approval of the Controller of Restrictive Business Practices to the proposed merger of the Israeli cable television operators, we cooperate with the other two Israeli cable television operators, among other things, in our marketing activities and entire content activities. In addition, as of December 2002, we and the other two Israeli cable television operators offer unified tiering packages (in the framework of which we changed the structure of the tiering packages we offer to our digital subscribers and the channels included in such packages).

When we started to provide our subscribers with digital broadcasting services we began signing new subscribers and those electing to purchase such digital services, on a new subscriber agreement. This agreement was approved by the Council in January 2001, together with the Council s approval of our digital broadcasting services. This agreement was submitted to the Standard Contract Court in Israel for its approval as required by law. In response to our filing this agreement for approval as a standard contract, the Ministry of Justice and the Israeli Council for the Protection of Consumers have submitted to this court a request that certain changes be made to our agreement. The parties have commenced negotiations for the purpose of reaching a version of the agreement that is acceptable to all the parties. In the event that the parties shall agree upon a version of the digital subscriber agreement, a notice shall be submitted by the parties to the Court. In the event that the parties shall not agree upon a version of the agreement, then a court procedure will be held. To date, a date has not been set for the court hearing. If the court approves our agreement, it may incorporate in it changes requested by the Ministry of Justice and the Council for the Protection of Consumers.

Additionally, when we started to provide our subscribers with access to High Speed Internet over cable services we began signing such subscribers on an access to High Speed Internet over cable agreement. This agreement was submitted to the General Administration of the Ministry of Communications for its approval as required by our Telecommunications Infrastructure License. To date, comments or amendments to this agreement of the General Administration have not been received. On October 27, 2002, this agreement was submitted to the Standard Contract Court in Israel for its approval as required by law. The Israeli Attorney General submitted to the Court a response to our filing this agreement for approval as a standard contract. A meeting was held with the representatives of the Ministry of Justice in the attempt to resolve the differences between the parties and to agree upon a version of the access to High Speed Internet over cable agreement. If the court approves our agreement, it may incorporate in it those changes requested by the Ministry of Justice. To date, a date has not been set for the hearing.

The terms that govern the use of our T-Mail and SMS services are presented to our subscribers on the subscribers television screens by way of reference to our Internet site and are subsequently sent by post to each customer that subscribes these services.

We also contact subscribers who request to be disconnected and attempt to rectify any perceived or actual problem promptly. Under the Telecommunications Law, and the subscriber agreement, we are required to disconnect an analog subscriber within 14 days of receipt of a written disconnection request, or such later date as the subscriber may request. According to our Cable Broadcast Licenses, we are required to disconnect a digital services subscriber within 2 business days of receipt of a written disconnection request or such later date as the subscriber may request and we must not charge the subscriber any fees from the date of the disconnection. According to our Telecommunications Infrastructure License, we are required to disconnect services provided under this License (which includes access to High Speed Internet over cable services) within 2 business days of receipt of a written disconnection request or such later date as the subscriber may request. During those periods, the marketing and sales groups contact the subscriber in an effort to retain the subscriber.

Although we seek to limit disconnections initiated by subscribers, a certain amount of such disconnections is inevitable, either because a subscriber has moved outside of our license areas or has decided that it no longer wishes to receive cable transmissions. We specifically focus on such homes that have disconnected cable services in our marketing efforts in order to get cable television subscriptions reinstalled by new subscribers who have moved into such locations or by subscribers who made a decision to no longer receive cable television services.

We believe that satisfaction with cable television services is essential in reaching and maintaining high levels of penetration. An integral part of our efforts has been to create for ourselves a positive image among our potential and existing subscriber base. To foster such image, we have been involved, and intend to continue to be involved, with various communities within our License areas by participating in public campaigns with local authorities.

Customer Service. We believe that highly efficient, responsive and prompt customer service is one factor in our marketing efforts to build and retain customer satisfaction. Since 1999, we operated a service number for the convenience of our subscribers. We currently operate a toll free number for our cable television subscribers. As of December 31, 2002, we had a staff of 228 customer service personnel on a full-time or full-time equivalent basis, which offers direct general and technical support via telephone or on-site. Customer service personnel are trained to provide general and technical support over the telephone in order to minimize the requirements for service and on-site support. However, if a problem cannot be resolved over the telephone, a service technician is dispatched to the location, usually at no cost to the customer. The customer support staff routinely provides feedback to the marketing and research and development groups. Since February 2002, our customer service personnel also engage in sales activities.

Franchises and Licenses. Between 1990 and April 2002, we conducted our operations pursuant to five exclusive franchises to operate cable television in central and northern Israel, including three of Israel s largest cities, and numerous smaller communities and rural areas. Pursuant to the terms of each franchise deed, we were granted the right to operate cable television systems in specified geographic regions, each of which included a densely populated metropolitan area and a less densely populated rural area. In 2002, these franchises were replaced by non-exclusive Cable Broadcast Licenses, a Telecommunications Infrastructure License and a Broadcasting HeadEnd License, to operate in the same geographical areas as the franchises. These licenses were granted on April 30, 2002, March 27, 2002 and May 2, 2002, respectively. As of December 31, 2002, the area covered by our non-exclusive Licenses was approximately 495,000 homes.

To maximize technological and administrative efficiencies, we currently operate the cable television services through four operational areas representing the areas covered by our previous franchises and new licenses: Bat-Yam/Holon, Haifa, Netanya/Hadera and Galilee (comprising of the Safed, Sea of Galilee, Kiryat Shemona and Golan Heights license areas). We operate two studios, which are located in Haifa and Bat-Yam, a common HeadEnd for the Kiryat Shemona, Safed and the Sea of Galilee license areas, which are included in the Galilee operating area, and a common HeadEnd for the Bat-Yam/Holon operating area. In order to further increase our technological and operational efficiencies, we intend to reorganize our current four operational areas in the near future, such that we shall operate through two operational areas, Netanya and Haifa.

A description of the areas where we currently conduct our operations covered by our Licenses are set forth below.

Bat-Yam/Holon: The Bat-Yam/Holon operating area includes the cities of Bat-Yam and Holon (which border Tel Aviv to the south) and neighboring areas. We completed installation of most of the cable transmission network in this operating area by the end of 1991. As of December 31, 2002, the area included approximately 114,500 households, and our network in the Bat-Yam/Holon area passed 114,479 homes and had 76,988 cable television subscribers.

Haifa: The Haifa operating area includes the city of Haifa and the surrounding communities. We substantially completed the installation of a regional cable transmission network in this operating area in 1995. As of December 31, 2002, the area included approximately 132,400 households, and our network in the Haifa area passed 127,816 homes and had 79,319 cable television subscribers.

Netanya/Hadera: The Netanya/Hadera operating area includes the coastal cities of Netanya, approximately 30 kilometers north of Tel Aviv, and Hadera, located between Haifa and Tel Aviv, and adjacent communities to these cities. We substantially completed the installation of a regional cable transmission network in this operating area in 1995. As of December 31, 2002, the area included approximately 191,200 households, and our network in the Netanya/Hadera area passed 166,220 homes and had 91,391 cable television subscribers.

Galilee: The Galilee operating area includes the city of Tiberias, along the Sea of Galilee, Safed and Kiryat Shemona, in Israel s north, as well as the surrounding small towns and agricultural communities, and the Golan Heights. As of December 31, 2002, the area included approximately 56,900 households, and our network in the Galilee operating area passed 49,487 homes and had 27,186 cable television subscribers. We have not completed the buildout of the cable network in this operating area.

The table below contains information on subscriber penetration in each of the four geographical areas in which we currently operate, as of December 31, 2002.

Area	**Date Commenced Cable Television Operations**	**Approx No. of Households**	**Plant Length (km)**	**Homes Passed**	**Cable Television Subscribers**	**Penetration Rate of Homes Passed(1)**	**Penetration Rate of Households (2)**	**Internet Subscribers**
Bat-Yam Holon	March 1990	114,500	586	114,479	76,988	67.3%	67.2%	5,437
Haifa	September 1991	132,400	1,108	127,816	79,319	62.1%	59.9%	6,974

Netanya Hadera	January 1993	191,200	3,218	166,220	91,391	55%	47.8%	8,113
Galilee	December 1990	56,900	1,130	49,487	27,186	54.9%	47.8%	1,325
Total		**495,000**	**6,042**	**458,002**	**274,884**	**60%**	**55.5%**	**21,849**

(1) Cable television penetration of homes passed is calculated by dividing the total number of cable television subscribers at applicable date by the total number of homes passed.

(2) Cable television penetration of households is calculated by dividing the total number of cable television subscribers at applicable date by the total number of households.

In order to further increase our technological and operational efficiencies, we intend to reorganize our current four operational areas in the near future, such that we shall operate our cable television services through two operational areas, Netanya and Haifa.

Technological Preparations for Competition in the Telecommunications Market

As part of our technological preparations toward becoming a multi-service operator for multi channel television broadcasting and interactive television, access to High Speed Internet over cable, telephony and data over cable services, we have completed the installation of an addressable analog broadcast system, a digital broadcast system and a data-over-cable platform.

The digital system has enabled us to provide our subscribers dozens of broadcasting channels, channel packages according to choice, Internet services, interactive services, and added value services, including Pay-Per-View and Near Video On Demand services (the latter of which we have not commenced).

As part of our preparation, the Company has defined, performed and completed a network upgrade project, for Segmentation and Bandwidth expansion.

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In order to enable fast two-way communication via cable modems, a split of the HFC network into smaller sub-networks, known as Segmentation , is necessary. The Segmentation project involves significant installation of new fibers and optical equipment. We completed the Segmentation process by the end of 2000 to the extent actually required to reflect our subscriber demand.

Our original network Bandwidth was 50-550MHz, and fully occupied 45-48 analog television channels. Full utilization of the network capacity is not possible due to regulatory restrictions. We have upgraded our network in order to expand the network capacity to 860MHz. The upgrade project included Bandwidth expansion of both the downstream and the upstream paths. The network s old equipment has been replaced, in all of our operational areas, by a new uniform type of equipment. The Bandwidth expansion increased the network capacity by approximately 25 analog channels, which is equivalent to more than 350 digital channels, and enabled Bandwidth allocation for new added value services.

The network Segmentation and Bandwidth expansion projects are part of our technological enhancement plan, which enables us to offer subscribers a new variety of interactive services, access to High Speed Internet over cable using, alternatively, the television screen or a personal computer, Pay-Per-View services, and may enable us in the future to offer telephony over cable and other Bandwidth consumer services.

We have completed a substantial portion of the construction of our cable television broadcast and transmission system, including technologically advanced HeadEnds and a broadband, hybrid optical fiber/coaxial cable television network. Our cable network consists almost entirely of underground plant. Our cable transmission network is capable of supporting both broadcast transmission and two-way data transmissions, for various telecommunications applications.

A cable television system begins with a HeadEnd, which transmits signals obtained from three main sources; satellite broadcasts received by dish antennae; local broadcasts received off-air or via optical transmission; and programs played back from video cassette recorders and/or video servers. A fiber optic cable network transmits signals carrying all the system s channels from the HeadEnd to secondary HeadEnds and distribution hubs, which cover the different areas of the licenses and service zones. From the secondary HeadEnds/hubs, the services are distributed to subscriber homes via coaxial network. The drop cable terminates at a wall outlet installed in the subscriber household; a cable from the wall outlet passes through a channel converter or a set top box to the subscriber s television set. A wireless remote unit enables the viewer to select a channel from among the broadcasted channels. Subscribers who own cable-ready television sets and prefer the analog services only, may connect their sets directly to the wall outlet and select the viewing channel via the television set s control panel/remote control.

In November 1989, pursuant to a special permit issued by the Ministry of Communications prior to our receiving a franchise, we became the first cable television operator in Israel to supply cable television services when we commenced operation of our HeadEnd in Bat-Yam. This HeadEnd currently includes a playback system and 11 parabolic antennas for reception of satellite broadcasts and serves the Bat-Yam/Holon operating area.

The subscribers in the Galilee operation area are served by a HeadEnd located at Ramot Naftali (completed in December 1990), which includes, among other things, a back-up play-back system and satellite dish antennas, cable-television programming is transmitted by microwave from the HeadEnd to 2 unattended sites, located in the Galilee operating area, which in turn is transmitted by underground cable to subscribers. Those microwave links have been progressively replaced by a modern fiber optics links.

In September 1991, we completed construction of a HeadEnd located in Haifa, which we now operate as our master HeadEnd. This HeadEnd includes, among other things, a playback system, satellite dish antennas and a production studio that generates original programming. Subscribers in the Haifa operating area are served by this HeadEnd via underground fiber optic and coaxial cables. A fiber-optic network carries television channels from the Haifa HeadEnd to the Netanya/Hadera operating area. The Haifa and Netanya/Hadera operating areas form a contiguous geographic area.

We acquired the HeadEnd equipment primarily from suppliers in the United States. Construction of the HeadEnds was for the most part carried out by sub-contractors supervised by a technical team from the Company. The HeadEnds are located on land that we either purchased or have leased under a long-term lease.

The cable installation includes several stages; preparation of an engineering plan and receipt of permits from local authorities, excavation, laying the cable and network installation (including connecting cables that have been laid and installation of network components); and repaving the area where the work was conducted.

The network installation for a given geographic area is deemed to have been completed when the infrastructure necessary to connect a building to the network has been installed adjacent to each of the buildings in the area. After completion of the network installation, network equipment is installed in the buildings in the relevant area and subscribers are connected to the system. As of December 31, 2002, we completed the installation of 3,755 miles of underground cable.

We supervise the various stages of network installation, which are performed by design, infrastructure and network contractors. We are not dependent on the services of any one of those contractors. In addition, we purchase equipment, including cable, from a number of foreign suppliers and are not dependent on any particular supplier. In building the network, we have left additional conduit space for future uses.

Cellular Telecommunication Services

As part of our strategy to develop and become involved in new telecommunication projects and become a leading telecommunication company in Israel, we became a shareholder in Partner Communications Company Ltd., the third of four providers of mobile cellular telephone services in Israel, and one of the two operators which use the GSM technology on a fully commercial basis in Israel.

In April 1998, Partner received its license to establish and operate a mobile telephone network in Israel. In October 1999, Partner completed an offering of its shares to the public, raising a gross sum of $525 million. Partner s shares are listed on Nasdaq, the London Stock Exchange and the Tel Aviv Stock Exchange, and Partner s debentures are listed for trade on the Luxembourg Stock Exchange. As a result of Partner s initial public offering we recorded capital gains in the amount of approximately NIS 447 million. In addition, Partner repaid its shareholder loans which it owed to us. In April 2002, we sold approximately 50% of our holdings in Partner to a subsidiary of Hutchison Whampoa Ltd., in consideration for $62,410,000. Currently we are the beneficial owner through Matav Investments Ltd. of approximately 7.42% of Partner s issued and outstanding shares. The other major beneficial shareholders in Partner are Hutchison Whampoa Ltd., Elron Electronic Industries Ltd. (through Elbit Ltd.) and Eurocom Communications Ltd. We have the beneficial right through Matav Investments Ltd. to appoint up to 2 directors to the board of directors of Partner (which is comprised of 17 directors) as long as we hold at least 4.99% of its issued share capital, pursuant to a shareholders agreement.

Approximately 72% of our current holdings in Partner are pledged to the banks participating in Partner s $710 million senior credit facility by means of pledges unlimited in sum, to secure Partner s undertakings under the credit facility.

On January 1, 1999, Partner commenced operations and the supply of services to the public on a fully commercial basis. Partner s GSM infrastructure covers approximately 97% of the Israeli population, and according to Partner s financial reports, the number of its subscribers as of December 31, 2002, is approximately 1.84 million, equal to approximately 29% of the total subscribers of cellular telecommunications in Israel.

Partner reported a revenue of approximately NIS 4,055 million in 2002 as compared to a revenue of approximately NIS 2,104 million and NIS 3,249 million in 2000 and 2001, respectively, and net income of approximately NIS 84.2 million in 2002 as compared to losses of approximately NIS 768.8 million and NIS 303.4 million in 2000 and 2001, respectively. Our share in the gains in 2002 amounted to approximately NIS 14.5 million, as compared to our share in the losses of approximately NIS 76.4 million in 2001 and NIS 126.5 million in 2000. Partner presents its financial statements in conformity with generally accepted accounting principles in the United States, or U.S. GAAP. Following adjustment to Israeli GAAP, Partner s results are reflected in our financial statements on an equity accounting basis and consequently have a material effect on our financial results.

International Telecommunication Services

On November 7, 1996, Barak I.T.C. (1995) The International Telecommunications Services Corp. Ltd., in which we indirectly hold a 10% share ownership interest, was granted a license to provide international telecommunications services in Israel. Barak and one other international telecommunications service provider license holder, 012 Golden Lines International Telecommunications Services Ltd., or Golden Lines, began offering international telecommunication services in July 1997. The other major beneficial shareholders in Barak are Clalcom Ltd., and indirectly, Sprint International, Inc., Deutsche Telekom AG and France Cables et Radio SA. We have the right to appoint 1 director to the board of directors of Barak (which is comprised of 11 directors), pursuant to a shareholders agreement.

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In July 2001, Barak and Golden Lines jointly applied to the Controller of Restrictive Business Practices in order to obtain his approval regarding a merger between the two companies. If agreed upon, the merger would be subject to entering into a comprehensive merger agreement and obtaining the approvals required under any applicable law or contract, including the approval of the Minister of Communications. We anticipate that following the merger, if a merger were to be consummated, the combined company would hold more than 50% of the international telecommunications market in Israel. This, in turn, may subject the combined company to additional regulatory scrutiny resulting from its dominant position in this market.

During 2002, Barak increased the total volume of voice traffic by approximately 16%. Since 1998, Barak has provided Internet services to its customers, and, according to Barak s management, as at December 2002, Barak holds a market share of approximately 24% of the business Internet market and approximately 10% of the residential Internet market in Israel. As of December 31, 2002, our investments in Barak totaled approximately NIS 16.6 million, after a write-off of approximately NIS 9 million of our investment in Barak (among other things, based on a company valuation of Barak). In November 1997, Barak issued senior subordinated discount notes, the proceeds of which amounted to $100 million. In addition Barak entered into loan agreements with two Israeli banks under which it was entitled to borrow up to $170 million. The availability period of the bank loans ended during November 2002. Barak reported revenue of NIS 708.0 million in 2002 as compared to NIS 570.5 million and NIS 686.9 million in 2000 and 2001, respectively, and net income of NIS 63.8 million in 2002 as compared to a loss of NIS 118.9 million and NIS 72.0 million in 2000 and 2001, respectively.

Since we have a 10% interest in Barak and our holdings in Barak are reflected in our financial statements on a cost basis, Barak s financial results do not affect our financial statements.

Investments in Technological Companies

In May 2000, we decided that together with other of our shareholders, we will invest in start-up companies which engage in fields of Internet, cable television, data telecommunications, applications, content, infrastructure and Internet Protocol telephony. To this end, Nonstop Ventures Ltd. was formed by several of our shareholders, in which we hold, as of November 2002, 50% of the issued share capital, following the exercise of an option granted to us under a memorandum of understanding dated December 31, 2000, as amended. Pursuant to the exercise of the said option, 50% of certain amounts we invested and loans we made on behalf of Nonstop Ventures Ltd. are deemed to be provided by us to Nonstop Ventures Ltd., in consideration of the issuance to us of a non-convertible promissory note by Nonstop Ventures Ltd., and the transfer and assignment to Nonstop Ventures Ltd. of our rights and obligations towards third parties in connection with such investments and loans. The shareholders of Nonstop Ventures Ltd. have agreed to finance its operations in proportion to their respective holdings up to a total sum of $15 million. Investments made by the respective shareholders in Nonstop Ventures Ltd. prior to October 30, 2002, are in consideration of the issuance to such shareholders of non-convertible promissory notes by Nonstop Ventures Ltd.

Through May 2000, and to May 31, 2003, we and the other shareholders have invested through Nonstop Ventures Ltd. in seven start-up companies an aggregate amount of approximately $5.8 million. Of the aggregate investment, we invested approximately $2.9 million. Due to, among other things, market factors, the financial situation of these companies and our accounting policies, these investment amounts were reduced in our financial records, and were set in our financial statements for the year ended December 31, 2001 at a value of approximately $1.4 million and were further reduced and set in our financial statements for the year ended December 31, 2002 at a value of approximately $0.6 million.

Government Regulation

General

The operation of cable television systems and other telecommunication services relating to our business is regulated in Israel by the Telecommunications Law, the Ministry of Communications, and the Council of Cable and Satellite Broadcasting.

The Council is established pursuant to the Telecommunications Law and is comprised of 13 members (including 6 representatives of the government and 7 representatives of the public) appointed by the Israeli Government upon the recommendation of the Ministry of Communications. The Council is authorized, among other things, to:

- grant cable broadcast licenses;
- establish policies and adopt rules concerning the type, subject and content of cable television programming;
- supervise the provision of broadcasting services by cable television and satellite operators; and
- advise the Ministry of Communications.

The Telecommunications Law and Our Licenses

Until we received our Licenses, we operated under 5 exclusive franchises in central and northern Israel. In July 2001, the Israeli parliament approved amendments to the Telecommunications Law, under which terms were set for the granting of licenses for the provision of telecommunication services via cable television networks, in place of the exclusive franchises. The amendments also set new regulatory standards with respect to television broadcasting services provided to subscribers in a highly competitive environment.

We now operate under non-exclusive long-term licenses pursuant to the provisions of the amended law. On March 27, 2002 we were granted a Telecommunications Infrastructure License by the Minister of Communications for the provision of infrastructure services for the distribution of cable broadcasts and access to Internet providers. On April 30, 2002 we were granted 2 Cable Broadcast Licenses by the Council. On May 2, 2002, we were granted a special license to hold a Broadcasting HeadEnd by the Minister of Communications. In November 2002, our Telecommunications Infrastructure License was amended by the Minster of Communications, pursuant to which we may provide additional infrastructure services of data communications, digital transmission and optic transmission services. The Licenses cover the same geographical areas as our previous five exclusive franchises.

The terms and conditions of the various regulatory approvals we have received to the proposed merger between the Israeli cable television operators also affect the regulation of our current business in certain respects. (See Section 4B: Arrangement for a Merger of the Cable Television Operators.)

Pursuant to the terms of the Telecommunications Law, as amended, and the terms of our Licenses, we are now subject, among other things, to the terms, conditions and restrictions set forth below.

Our Licenses

Corporate Separation of Cable Broadcast and Telecommunications Infrastructure Licensees

We must operate through separate entities, namely the broadcast entities, on the one hand, and an infrastructure entity, on the other hand, which must each hold a License for Cable Broadcast or Telecommunications Infrastructure, as appropriate. Pursuant to the Telecommunications Law, the Telecommunications Infrastructure Licensee must own the cable network infrastructure as a condition to the receipt of the License. However, according to an agreement with the Ministry of Communications incorporated in our Telecommunications Infrastructure License, our Cable Broadcast Licensees are allowed to continue to own the cable network infrastructure and to provide infrastructure services for an additional interim period of the earlier of two years following the date of the grant of the Telecommunications Infrastructure License (i.e. until March 27, 2004), or the date of the consummation of the merger of the Israeli cable television operators. During such period, the necessary arrangements must be made regarding the transfer of the ownership of the cable network infrastructure to the Telecommunications Infrastructure Licensee. Accordingly, and as a condition for the receipt of the Telecommunications Infrastructure License, our Cable Broadcast Licensees and our Telecommunications Infrastructure Licensee entered into an agreement dated March 5, 2002, whereby our Cable Broadcast Licensees granted an exclusive lease to our Telecommunications Infrastructure Licensee for the right to operate the cable network infrastructure. At the end of the lease period, ownership of the cable network infrastructure shall be transferred to our Telecommunications Infrastructure Licensee (or to the merged entity), and the Telecommunications Infrastructure Licensee (or the merged entity), shall be the exclusive owner of the cable network infrastructure in accordance with the relevant Licenses and applicable law. In October 2002, our Cable Broadcast Licensees and our Telecommunications Infrastructure Licensee entered into an agreement, whereby the Telecommunications Infrastructure Licensee shall provide the Cable Broadcast Licensees infrastructure services for the broadcast of cable broadcasts in the areas covered by their respective license, including installment, maintenance and disconnection of terminal equipment.

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The Cable Broadcast Licenses and the Telecommunications Infrastructure License all contain restrictions limiting the number and identity of directors that are permitted to serve in both the Infrastructure entity (and its general partner), and the Cable Broadcast companies.

In the event that either another entity is granted a general license to broadcast through our cable network infrastructure, or in the event that we reach a number of subscribers to our access to High Speed Internet over cable services equal to 45,000, the separation rules set forth below shall apply. Subject to the aforesaid, the Council and the Minister also have the authority to impose conditions in addition to those set forth below, regarding the relationship between the Cable Broadcast Licensees or the Telecommunications Infrastructure Licensee and their connected companies, including the identity of the officers of each company, the transfer of information, the separation of entities between broadcast and infrastructure, the accounting systems, and technological, geographical or commercial restrictions regarding the laying down of infrastructure or regarding the provision of services or broadcasts.

Separation rules:

i. A separation must be effected between the management of the Cable Broadcast Licensees, on the one hand, and the management of the Telecommunications Infrastructure Licensee and the general partner of such Licensee (but not including the board of directors), on the other hand, including in relation to the business, financial and marketing systems;

ii. subject to the interim period mentioned above, a division of the assets of both Cable Broadcast Licensees and the Telecommunications Infrastructure Licensee must be effected;

iii. the Telecommunications Infrastructure Licensee and its general partner shall not be permitted to employ the employees of the Cable Broadcast Licensees and vice versa; and

iv. our Telecommunications Infrastructure License stipulates that no employee of both the Telecommunications Infrastructure Licensee and its general partner can also be a director of either Cable Broadcast Licensee, if pursuant to such employee s duties he has access to commercial information regarding any other general broadcast licensee that competes with our Cable Broadcast Licensees.

In the event that a company connected to the Telecommunications Infrastructure Licensee is an Internet service provider, then there will be an immediate obligation of structural separation with relation to the Telecommunications Infrastructure Licensee and the *Internet* service provider, in accordance with the above restrictions.

Terms and conditions that are common to our Cable Broadcast and Telecommunications Infrastructure Licenses

Term of our Licenses

Our Cable Broadcast Licenses and our Telecommunications Infrastructure Licenses are each valid for initial periods of 15 years. The Cable Broadcast Licenses and the Telecommunications Infrastructure Licenses may be extended for additional 10-year periods, by the Council and the Minister respectively, upon the request of the Licensees. Our Broadcasting HeadEnd License is valid for as long as our Cable Broadcast Licenses are valid, but no later than May 30, 2017. It may be extended further upon request to the Ministry of Communications.

In order to have our Licenses extended, we are obliged to prove, during the terms of the Licenses, that we have met with their terms and conditions. To this end, we are required to deliver detailed reports to the Council as to our compliance with our Cable Broadcast Licenses and applicable law, and evidence of acts that we have taken to improve the quality and technology of the broadcasts. We are similarly required to deliver detailed reports to the Minister in respect of the Telecommunications Services.

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Guarantees

In order to ensure compliance with our obligations pursuant to the new Licenses, applicable law and regulatory bodies, and to ensure payment of fines that may be imposed by the Council and the Ministry, we have provided:

a guarantee of $10 million to the Ministry of Communications pursuant to the Telecommunications Infrastructure License; and

a guarantee of NIS 9 million to the Council pursuant to the Cable Broadcast Licenses.

Each of the Minister and the Council has the authority to exercise the applicable guarantees in the event that the Licensee does not fulfill its obligations, and to cover any damage, loss or cost that the Council, the Minister, or the government may incur as a result of any breach of our obligations under the Licenses, and to ensure any payments by the Licensee, including royalty payments and payments of fines imposed by the Council or the Minister. The exercise of the guarantee does not derogate from the authority of the Council or the Minister to cancel the Licenses, to amend the terms and conditions of the Licenses or to impose other sanctions including fines for certain stipulated breaches or actions.

Subscriber Services

We must provide our infrastructure services to all applicants in our service area, upon non-discriminatory terms. We are obliged to connect anyone wishing to be a subscriber of our cable broadcast services or our infrastructure services according to the terms of our relevant License, within stipulated time periods.

Our standard subscriber agreements are subject to the approvals of the Council (regarding the cable broadcast subscriber agreement), the Ministry of Communications (regarding the access to High Speed Internet subscriber agreement), and the Court for Uniform Contracts. We may be directed to amend the terms of our standard subscriber contracts.

Our infrastructure company is obliged to offer its services to all applicants, regardless of whether or not they may be a subscriber of another licensee (including a broadcast licensee). We are prohibited from making the provision of our infrastructure services dependant upon the purchase of our own or another s services, or dependant on not receiving services from another, unless authorized to the contrary by the Minister.

We are prohibited from making the supply of broadcasts dependant upon unreasonable, discriminatory or unfair terms, such as: minimum periods; or the receipt of other services; or the obligation to obtain equipment from another or us. We are prohibited from discriminating between subscribers. We are also subject to rules concerning the time limits allowed for connection and disconnection of subscribers, after such subscriber has given us notice.

We must continue to operate a customer service call center and office, for technical and general customer support, and appoint a complaints officer. Minimum standards are set in our Licenses as to the operation of such services and the management of customer complaints.

We do not have the right to disconnect or discontinue our broadcast and infrastructure services except: upon the subscribers request, for a material breach of agreement, for the purpose of maintenance, or due to risk, or as further set forth in our Cable Broadcast Licenses and Telecommunications Infrastructure License.

Restrictions upon Transfer of Assets

According to the Telecommunications Law, the licenses themselves and any rights granted thereunder may not be charged, transferred, or made subject to a lien, with the exception of transfers within the framework of structural reorganizations. Both Cable Broadcast Licenses and the Telecommunications Infrastructure License also stipulate that the assets of the Licensees pertaining to the Licenses (including Terminal Equipment of the Cable Broadcast Licensees) may not be transferred, assigned, charged or otherwise pledged in any way, other than in accordance with the provisions of the Telecommunications Law (in respect of the Cable Broadcast Licenses), and only upon advanced written consent of the Minister (in respect of the Telecommunications Infrastructure License). However, according to the Telecommunications Law, it is possible to create a charge upon the assets of a cable broadcast licensee in favor of a bank legally operating in Israel.

In addition, the Telecommunications Infrastructure License states that the Telecommunications Infrastructure Licensee is allowed to create a charge in favor of a bank legally operating in Israel in order to receive financial credit, provided that prior notice is given to the Minister of Communications, and so long as the charge agreement includes a provision according to which the exercise of rights pursuant to the charge shall not be harmful to the provision of services by the Telecommunications Infrastructure Licensee.

Restrictions upon Ownership and a Change of Means of Control.

According to the Telecommunications Law, a cable television operator must be a citizen and a resident of Israel, or an entity incorporated in Israel, and at least 26% of any means of control of such entity must be held by Israeli citizens and residents.

According to our Cable Broadcast Licenses, the Council s authorization is necessary for any of the following changes of means of control in a Cable Broadcast Licensee, and any such change effected without the Council s authorization shall be void.

(i) a change of identity of the controlling entity of the Cable Broadcast Licensees;

(ii) an increase in shareholding over 10% in the Cable Broadcast Licensees;

(iii) a change in the holdings of the Cable Broadcast Licensees following which any party becomes an interested party (a holding of 5% or greater), or have a material influence (a holding of 25% or more); or if such party has ceased to be such an interested party or holder of material influence;

In addition, any agreement pledging the controlling shareholding must be conditional upon the Council s approval, if this would cause a change in the means of control of the Cable Broadcast Licensees.

These restrictions outlined above must also be entrenched in the articles of association of the Cable Broadcast Licensees (not applicable to a change of means of control in connection with a transfer of shares publicly traded on a stock exchange). Our shareholders resolved at our last annual general meeting to amend our articles of association to reflect these restrictions. According to our Telecommunications Infrastructure License, the authorization of the Minister is necessary for any of the following changes of means of control in the Telecommunications Infrastructure Licensee:

(i) if any party becomes an interested party (a holding of 5% or greater);

(ii) if any party gains a material influence (a holding of 25% or more);

(iii) if any party becomes a controlling shareholder;

(iv) if any party ceases to be such an interested party, or holder of material influence, or controlling shareholder.

Further, in the event that a charge is placed over the means of control of the Telecommunications Infrastructure Licensee or over the means of control of an interested party of the Licensee, which, if exercised will make the grantee a holder of 10% or more of any means of control in the Telecommunications Infrastructure Licensee, or become a controlling shareholder, then such charge must include a provision stating that the exercise of the charge is conditional upon receipt of consent from the Minister of Communications.Due to restrictions regarding cross ownership interests, certain entities or individuals are prohibited from becoming an interested party in the Telecommunications Infrastructure Licensee.

According to our HeadEnd License, the prior written approval of the General Administration of the Ministry of Communications is necessary for the transfer of the License, directly or indirectly, to another. For this purpose, transfer shall include a change in the holdings of the means of control of the Licensee, even if this does not include a change of identity of the controlling entity of the Licensee.

For information regarding our applications for the approval of the Minister, the Council and the General Administration of the Ministry of Communications to the indirect transfer of our means of control, see Item 4C. Organizational Structure .

Specific Terms and Conditions of our Cable Broadcast Licenses

In addition to those mentioned above, our Cable Broadcast Licenses also include, among others, the following specific terms and conditions.

Subscription fees

The subscription fees that we charge for cable television services are regulated under the terms of our Cable Broadcast Licenses and by regulations promulgated under the Telecommunications Law. Pursuant to such regulations, the fees are linked to the Israeli consumer price index. If the consumer price index increases between 4% and 10% after the date of a previous increase of the fees and rates we charge, then we can increase fees and rates once every 3 months. However, if the consumer price index increases in excess of 10% after the previous increase of our fees and rate charges, then we may increase fees and rates regardless of whether three months have passed since the previous increase of such fees and rates. We are authorized to charge subscribers a monthly subscription fee, fees for the Premium Broadcastings, fees for Pay-Per-View services, an installation fee, lease payments or a deposit for the set-top boxes, an additional outlet fee and fees for certain ancillary services. We are subject to maximum charge restrictions for the deposit for the digital set-top boxes, which must not equal more than the value of the set-top box at the time of the deposit. In addition, we must not charge an aggregate fee for the lease of the set-top box equal to more than the value of the set-top box. With the exception of the deposit collected for the loan or lease of terminal equipment (such as set-top boxes) to the subscriber, we are prohibited from collecting guarantees or other securities from the subscriber. We are permitted to deduct 10% per year or part of a year, from the deposit for the set-top box. In accordance with an amendment to regulations promulgated under the Telecommunications approved by the Economic Committee of the Israeli parliament on June 16, 2003, the deduction from the deposit for the set-top box is 10% of the value of the set-top box. The Economic Committee of the Israeli parliament also resolved on June 16, 2003 to approve a further amendment to regulations promulgated under the Telecommunications Law, which regulates the ability of the Cable Broadcast Licensees to lease the set-top box to the subscriber, at the subscribers choice, in accordance with the terms of the Cable Broadcast License, and in addition, and in addition, pursuant to this amendment, Cable Broadcast Licensees are also allowed to sell the set-top boxes to subscribers, at the subscriber s choice, in consideration of an amount that shall not be more than the value of the set-top box.

Our Cable Broadcast Licenses stipulate that we may not charge our analog subscribers for the basic broadcasts more than approximately NIS 148 plus VAT, in the Holon/Bat Yam and Haifa/Hadera regions, approximately NIS 140 plus VAT, in the Sea of Galilee/Netanya region, and approximately NIS 141 plus VAT, in the Golan/Sefat and Kiryat Shemoneh region. Additionally, we may not charge our analog subscribers for a movie provided on a Pay-Per-View basis more than approximately NIS 15 plus VAT. Such fees may be linked to the Israeli consumer price index from February 2002. Our Cable Broadcast Licenses do not stipulate fees for digital subscribers. Under regulations promulgated pursuant to the Telecommunications Law, we may determine our subscriber fees for digital subscribers (including the basic broadcasts package). Such fees that we set for our digital subscribers must be reasonable, and the Minister may direct us to amend such fees if he finds, among other things, that they are harmful to competition, discriminatory or misleading.

We have the right to offer discounts and make special offers for limited periods, subject to giving prior notice to the Council and the Ministry. They have the combined authority to disallow or direct us to take actions with regard to any offers that we wish to make, upon specific considerations set forth in our Cable Broadcast Licenses. In the event that such offers last for longer than the limited period allowed, the Council has the authority to deem the sale prices to be a request to amend our price list accordingly.

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Broadcasts and Programming

Pursuant to the terms of our Cable Broadcast Licenses, the Cable Broadcast Licensees shall air only the broadcasts that have been authorized by the Council, according to the terms of such approval. Such broadcasts shall be both digital and analog, or any other system authorized in advance by the Council. We may request permission to reduce the scope of the analog broadcasts, and in such event, we may be instructed to charge lower subscription fees. We are prohibited from ceasing the supply of approved programs or packages without the Council s prior approval. The Council has the authority to change the terms of its approval of broadcasts, and shall have the authority to cancel the approval for the broadcast of any channel following breach of the terms of the approval, or to a material change in the content of the channel.

We are required to provide a stipulated amount of independent and local original programming, including information and broadcasts/programs exclusively regarding events in local areas, as well as a variety of films, and entertainment, music, arts, education, science, culture and sport programming material, all in accordance with quantity and content criteria established by the Telecommunications Law, our Council Regulations and our Cable Broadcast Licenses. We are also required to provide real time, unedited transmission of radio and television programming broadcasts to the public in Israel, receivable from the open airwaves, including those of foreign television stations and educational television broadcasts. We must provide an electronic programming guide. Recently, the Council published a draft of a proposed Council decision regarding a proposed amendment to the current obligations of the Cable Broadcast Licensees in respect of the content and scope of broadcasts that the Licensees are required to provide, which, if approved, would reduce our current obligations.

Our Cable Broadcast Licenses prohibit us from conditioning (directly or indirectly) the provision of any broadcasts to a subscriber upon the purchase of other broadcasts, including by means of unreasonable pricing (which shall be in the opinion of the Council, unless explicitly approved in advance by the Council). However, this does not affect our ability to condition the receipt of additional digital broadcasts upon the purchase of the digital basic broadcasts package. The Council may, for special reasons, direct us to alter the composition of the tiering packages, or to separate a channel from the basic packages. We are obliged to allow subscribers the right to purchase individual channels separately, although if the Council is convinced that we are offering our subscribers a broad choice at reasonable prices, it has the authority to exempt us from this latter requirement.

Our Cable Broadcast Licenses stipulate a limitation upon the amount of broadcasting time that may be dedicated to reruns in Channels 3, 4, 5 and 6 (family, movies, sports and children, respectively). We are prohibited from advertising new broadcasts, channels, or packages before we have served the Council with a request to broadcast such broadcasts, channels or packages. The Council has the authority to prohibit such advertisements until such request is granted. Further, any offering of free broadcasts to subscribers must include an express clarification, to be approved by the Council in advance, as to our plans to charge subscribers for such broadcasts in the future.

We are entitled to broadcast notices regarding sponsorships into certain sports broadcasts, subject to certain conditions, in accordance with and as set forth in the Council s decision of September 3, 2002.

In accordance with the Council s decision of June 2002, as amended in September 2002 and May 2003, each Cable Broadcast Licensee is required to allocate to production or purchase of locally produced broadcasts, a percentage of its annual income derived from subscriber fees for the year preceding the year of the investment, as follows: (i) commencing April 30, 2002 (the date of the grant of the Cable Broadcast License) and until the end of 2005, at least 8% of such income; and commencing 2006 and thereafter, as to be determined by the Council prior to the end of June 2005; and (ii) in the event a Cable Broadcast License is granted to the merged entity of the Israeli cable television operators, the Council shall determine, prior to the end of June 2005, the rate of the amounts that shall be allocated to local productions by the Cable Broadcast Licensee as of 2006. For this latter purpose, the Council shall consider, among other things, the financial condition of the Licensees in connection with their broadcast activities and the contribution of the merger to the improvement of the financial condition of the Licensees.

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Obligation to Broadcast Specific Channels of Special Broadcast License Holders

Our Cable Broadcast Licenses stipulate that we must allow any holder of a special broadcast license to broadcast a specific channel to have access to our subscribers. Restrictions apply to the terms of any agreement with the holder of the special broadcast license, to the effect that such terms cannot be inferior to the terms on which we broadcast our own channels. The obligation to allow such access does not apply to analogical broadcasts, with the exception of dedicated channels or channels that were broadcast on the analogical system before the granting of the general non-exclusive license (such as the Shopping Channel). We shall be required to commence the broadcasts of such a special broadcast license holder at any time, or upon such date that the Council shall direct, even if no agreement has been reached with such a special broadcast license holder, and even if we have been unable to reach agreement as to the price, provided that such special broadcast license holder will provide guarantees.

In any advertisement of the broadcast schedule of the independent channels, a special broadcast license holder shall not be discriminated against by the Cable Broadcast Licensee. The fee that we are permitted to charge for such broadcasts shall include costs in addition to reasonable profit for such inclusion of information in such advertisement. We must include broadcasts of a special broadcast license holder on the electronic programming guide, and we must air trailers for such broadcasts. We shall also be responsible for taking any specific actions necessary to enable broadcasts of the special broadcast license holder, including the provision of technical services upon terms equal to those provided to its independent channels. The price for such services shall be included in the general fee for the broadcast. We shall be obliged to connect subscriber(s) to channels of a special broadcast license holder within 3 days of notification by the special broadcast license holder and the special broadcast license holder is entitled to elect whether to offer its broadcasts to subscribers as part of a package of channels of such special broadcast license holder or of other special broadcast license holders, in addition to the offer of its broadcasts to subscribers as a single channel. We are prohibited from preventing such choice from being effected.

Outstanding obligations from the previous franchises

Our Cable Broadcast Licenses, as amended by the Council s decisions dated April 10, 2003, list all of the following unfulfilled obligations on behalf of all of the previous franchise holders in Israel, which are still outstanding under the terms of the previous exclusive franchises. Based upon the number of subscribers, our pro rata portion of the cost of such common obligations would be approximately 25%. During a period of 8 years commencing two years from the date of our Cable Broadcast Licenses, we and the other cable television operators are obliged to fulfill these obligations. In accordance with the Council s above said decision, the total outstanding obligations include:

i. 398 hours of original locally produced broadcasts;

ii. $6,382,178 worth of investments in original locally produced broadcasts;

iii. 3,890 hours in total of original programming in Channels 3, 6 and 8;

iv. 342 movies in Channel 4;

v. 5,483 regional news broadcasts of at least 15 minutes each; and

vi. 1,468 hours of programs with translations into sign language for the hearing impaired.

The cable television operators and the Council have corresponded in connection with the outstanding obligations as determined by the Council, in connection with which on May 6, 2003 a letter was sent to the Council on behalf of the Israeli cable television operators that expressed an objection to the Council s above decision with regards to the outstanding obligations as determined by the Council.

Specific terms and conditions of our Telecommunications Infrastructure License

In addition to the above, our Telecommunications Infrastructure License also include, among other things, the following terms and conditions.

Services

According to our Telecommunications Infrastructure License, we have the right to grant general cable broadcast license holders services with connection to their use of our network infrastructure, and to provide services of access to High Speed Internet over cable.

The provision of our service to a broadcast licensee shall be effected in such a manner that the broadcast licensee shall be able to provide its services to the subscribers in accordance with the terms and conditions of its license. We must provide our services on reasonable and equal terms to all licensees, unless authorized otherwise by the Minister, in writing. We are prohibited from allowing any preferential service to any company linked to our Telecommunications Infrastructure Licensee.

Fees

According to our Telecommunications Infrastructure License, the fees we are permitted to charge our subscribers include: payment of installation fee for connection; payment for terminal equipment and installation thereof; payment for installation of extensions; relocation fees; payment for the sale, loan or lease of terminal equipment; regular periodic payments; varying payments for use of the service according to time or traffic volume; and payment for conversion of services. With the exception of a deposit collected for the loan or lease of terminal equipment (such as cable modems), we are prohibited from collecting guarantees or other securities from subscribers. We may deduct from the deposit for terminal equipment an amount of up to 10% for each year or part thereof.

We have the right to determine service packages of telecommunications services that we provide, at an overall price per package of services, or a price for each service. We are obliged to offer, without discrimination, every service and every service package on equal terms and at a uniform fee, according to the type of subscribers in every service area. We must make information with respect to fees fully available to every applicant, including on the Internet.

We are obliged to notify the Ministry in advance of any intended changes in fees. The Minister has the right to alter the fee if he finds that it contravenes the provisions of the license or might compromise competition or the subscribers.

When collecting payment from a subscriber for another service provider, no addition shall be charged to the other entity s fee.

Ownership of the Network

Our Telecommunications Infrastructure Licensee shall be (upon termination of the interim period) the owner and operator of the network. We have the exclusive right to operate the network.

Frequencies

Certain frequency bands are forbidden, including between 806MHz and 862 MHz. We are prohibited from causing interference to other systems and shall cooperate in preventing interference.

Our Broadcasting HeadEnd License

Term

Our Broadcasting HeadEnd License is valid for as long as our Cable Broadcast Licenses are valid, but no later than May 30, 2017, although we may request for it to be extended beyond this date. The General Manager of the Ministry of Communications has the authority to conduct inspections to ensure that the terms of our Broadcast HeadEnd License has been complied with.

Purpose

This License allows us to among other things; construct, maintain and operate of broadcasting HeadEnd, for the purpose of maintaining the cable services provided by the Cable Broadcast Licensees; to connect our telecommunication system to the public telecommunications network operated by our Telecommunications Infrastructure Licensee or another entity licensed for transmission; to connect our telecommunications system to the system of another special licensee for operating a HeadEnd, to enable broadcasting reception via our telecommunications system and to construct and operate monitory mechanisms needed to ensure the orderly operation of our telecommunications system. In October 2002, two of our Cable Broadcast Licensees entered into an agreement, pursuant to which one Licensee will provide the other HeadEnd services for the purpose of transmission of cable broadcasts.

The status of our Licenses in the event that the merger between the Israeli cable television operators is consummated

Cable Broadcast License: In the event that the merger between the Israeli cable television operators is consummated, the merged entity must apply to the Council for a new Cable Broadcast License. The terms of the approval of the Council to the merger (dated March 7, 2002, as amended on February 13, 2003) shall be incorporated into any new broadcast license that will granted to the merged entity and that will replace our current Cable Broadcast License.

Telecommunications Infrastructure License: the Minister may, if the merger is consummated, replace the Telecommunications Infrastructure License and grant a new license to the merged infrastructure entity. Given that it is envisaged that the scope of services provided by the merged entity shall be materially broader than the services we currently offer our subscribers, including telephony services, the terms of the new license shall be determined in accordance with such increased services and other considerations as determined in the Telecommunications Law. However, in the event that the merger is not consummated within 2 years of the grant of the License (March 27, 2004), then the Minister shall consider the need to amend the existing License conditions in order to make them suitable for the situation at that time, in particular regarding the fact that there is no merged entity and the possibility to increase the Licensee s services in the absence of such merged entity.

Royalties and Payments to the State of Israel

Under our Cable Broadcast Licenses, we are required to pay the Ministry of Communications an annual license fee and a variable royalty. The variable royalty is payable quarterly in an amount equal to a certain percentage of our annual gross revenues (not including V.A.T.) from the provision of certain broadcast services, which include, among other things, certain installation and subscribers fees. (Regarding revenues derived from subscriber fees for tiering and pay-per-view broadcasts, such revenues shall be calculated for the purpose of payment of royalties net of payments that the licensee is contractually obligated to pay to the holder of the rights to such broadcasts.) Under amendments to regulations promulgated under the Telecommunications Law proposed by the Minister of Communications and approved by the Economic Committee of the Israeli parliament on June 16, 2003, royalties payable by Cable Broadcast Licensees have been reduced, effective retroactively, from 5% of our annual gross revenues (not including V.A.T.), to 4% of such revenues in 2002 and 2003, and 3.5% of such revenues from 2004. For information regarding a petition filed in the Israeli Supreme Court of Justice in connection with the approval of the Economic Committee of the Israeli parliament to the said proposed amendments, see Item 8A. Consolidated Statements and Other Financial Information - Legal and Arbitration Proceedings .

In addition, regulations promulgated under the Telecommunications Law provide for royalties payable by general telecommunications licensees (which includes our Telecommunications Infrastructure Licensee) for the right to provide local fixed line communication services (including access to high speed Internet), as follows: until December 31, 2003, 4% of certain income, and from January 1, 2004, 3.5% of certain income. Certain income for these purposes includes all income of the general telecommunications licensee that is derived from the provision of telecommunications services pursuant to its license, excluding:

i. income collected by the licensee on behalf of another licensee (general or special) and transferred to the said other licensee; or payments made to a different general license holder for the completion of calls, or the transfer of such calls in the telecommunications network of such other license holder, including payments made for interconnection;

ii. income of the licensee from the provision of transmission services to other license holders;

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iii. income of the licensee from segments of transmission services by way of satellite;

iv. income of the licensee from selling terminal equipment; and

v. bad debts that are related to income from the provision of services in relation to which the licensee pays royalties.

Our Broadcasting HeadEnd License determines that the Licensee shall pay fees in consideration for the License as determined by the Ministry of Communications pursuant to the Telecommunications Law and the Telegraph Ordinance [New Version], 1972.

According to the agreement with the State of Israel of July 2001, each cable television operator is also obliged to make payments to the government over a period of 12 years commencing on January 1, 2003, equal to its pro rata portion of a sum determined by multiplying certain accumulated income of all the cable television operators, including certain income derived from the use of cable infrastructure, by a percentage which is between 0% and 4%, increasing gradually according to the amount of the certain income. (In the July 2001 agreement, it was agreed that our pro rata portion would be 24.1%, until agreed differently by all of the cable television operators.) Further, each cable television operator must pay the State of Israel in the 12-year period up to 12% of its income from the sale of any activity related to the cable infrastructure or a right related to such activity, and the sale of certain assets as set forth in the agreement. These provisions shall continue to be in effect if the cable television operators effect the merger. In March 2003 the cable television operators approached the Israeli Ministry of Finance with a request to defer for one year the commencement of payments due under the July 2001agreement, and this matter is currently under discussion. In a meeting with the Israeli Ministry of Finance on April 30, 2003, the Ministry of Finance demanded that should the merger of the Israeli television operators be consummated, the July 2001 agreement will be adjusted to correspond with the new organizational structure following the merger, such that the merged cable infrastructure entity shall also become a party to the July 2001 agreement, and the provisions of such agreement regarding the proportional amounts of the cable television operators in the joint consideration to be paid to the State of Israel under such agreement shall be adjusted such that the merged cable broadcast entity and the merged infrastructure entity shall be severally and jointly responsible for the entire joint consideration due under such agreement.

ICP and Cooperation of Cable Television Operators in Production of Broadcasting

In 1989, we, together with the other Israeli cable television operators, formed I.C.P. Israel Cable Programming Company Ltd., or ICP , for the purpose of jointly purchasing and producing our local cable channels, which then consisted of four channels: family, movies, sport and children. The culture & science channel was later added. We currently hold approximately 25% of the outstanding share capital of ICP.

In January 1995, the cable television operators and ICP reached a settlement with the Controller of Restrictive Business Practices regarding the operation of ICP, according to which, among other things, ICP shall produce, create or acquire at least 15% of its programming from local agents and suppliers.

Today, ICP creates, produces and acquires content for two channels (family and movies) and independent producers produce the other three channels in accordance with the Restrictive Business Practices Court decision in 1996 in connection with the approval of the ICP settlement.

After several temporary extensions of the ICP settlement, on July 6, 2000, the Restrictive Business Practices Court approved the extension of the ICP settlement until March 22, 2002, in accordance with terms and conditions of the Council, that were agreed to by the cable television operators, including an obligation to allow YES to broadcast the family, movies, sport and children s channels for consideration.

According to Council decisions in March 2002, May 2002 and December 2002, the Council further extended the ICP settlement until June 30, 2003, subject to the obligation to allow YES to broadcast those channels for consideration, excluding originally produced content, until the earlier of either: December 31, 2003 (regarding the family, movie and sports channels), and March 1, 2003 (regarding the children s channel); or the date upon which YES has at least 500,000 subscribers. After the expiry of this obligation upon the cable television operators, YES may request an extension. The obligation regarding the children s channel has since expired. YES broadcasts the family channel produced by ICP. YES ceased to broadcast the movie channel produced by ICP on June 30, 2002. Furthermore, pursuant to the Council s decision in March 2000, we are prohibited from broadcasting content that we purchased on an exclusive basis (with the exception of originally produced content).

Under the approval of the Controller of Restrictive Business Practices to the proposed merger of the Israeli cable television operators, it is no longer necessary for the activity of ICP to be subject to the approval of the Restrictive Business Practices Court. However, the terms and conditions of the approvals of the Council to the proposed merger impose on the merged entity similar provisions to those that currently apply to ICP regarding the broadcasting obligations towards YES. For additional information regarding the conditions of the approvals for the proposed merger, see Item 4B: Agreement for a Merger of the Cable Television Operators .

For information regarding certain guarantees we have provided to two banks to secure certain liabilities of ICP, see Item 5B. Operating and Financial Review and Prospects - Liquidity and Capital Resources .

For information regarding two law suits filed in the District Court of Los Angeles, California, United States, by Warner Bros. International Television Distribution, a provider of movie and series content broadcasted on the family and movie channels of the Israeli cable television operators, including ours, against the two other Israeli cable television operators, Tevel Israel International Ltd. (or Tevel) and the Golden Channels & Co. (or Arutzi Zahav), alleging that these cable television operators are in breach of their respective license agreements with Warner Bros, see Item 8A - Consolidated Statements and Other Financial Information - Legal and Arbitration Proceedings . These lawsuits could affect, among other things, the content which is broadcasted on channels of the Israeli cable television operators, including the content broadcasted on cable channels produced by ICP, and the Israeli cable television operators, through ICP, are currently holding negotiations regarding the purchase of content in place of the Warner Bros. content. Further, on June 30, 2003, an agreement was entered into by and between us and Cable Systems Media Haifa-Hadera Ltd., Tevel and two of its affiliated companies (collectively referred to as Tevel), Arutzi Zahav and two of its affiliated companies (collectively referred to as Arutzi Zahav), and I.C.P. Israel Cable Programming Company Ltd., under which each of the cable television operators undertakes to participate in amounts which Tevel and/or Arutzi Zahav will be required to pay to certain major producer companies in connection with legal proceedings (including the two lawsuits currently pending mentioned above) in respect of agreements regarding the purchase of content (used by all three cable television operators) entered into with such major producer companies, by each of Arutzi Zahav (for the family channel) and Tevel (for the movie channel and the pay movie channels, namely Cinema 1, 2 and 3 and Cinema Prime), all pursuant to a Court ruling rendered in the framework of such legal proceedings, and the legal expenses of Tevel and Arutzi Zahav in connection with such legal proceedings. The amount which each cable television operator will be required to pay of the amounts due shall be proportionate to the number of subscribers of such cable television operator in relation to all of the subscribers of the cable television operators, all at the time of payment.

Agreement for a Merger of the Cable Television Operators

In February 2003, the other Israeli cable television operators and us agreed on a final version of an agreement, which sets forth the structure and conditions of a merger between us and the other Israeli cable television operators. The parties have agreed that this merger agreement, upon its signing, will be added to and broaden the terms of the previous arrangement between these parties executed on December 31, 2001 (further to previous arrangements between the parties dated December 29, 1999 and April 30, 2001 that were cancelled and replaced). In the event any terms of these agreements shall conflict, the terms of the latter agreement of February 2003 shall prevail. Under the terms of this merger agreement, on the date of the consummation of the merger, all of our cable broadcast operations will be transferred to our subsidiary, Cable Systems Media Haifa-Hadera Ltd., immediately following which all of the cable broadcast operations of the cable television operators shall be merged into and together with Gvanim Cable TV Ltd., such that Gvanim Cable TV Ltd. shall become the merged broadcasting entity. Likewise, all of the infrastructure operations of the subsidiaries of the cable television operators shall be merged into and together with a wholly owned subsidiary of Gvanim Cable TV Ltd., such that this subsidiary of Gvanim Cable TV Ltd. shall become the merged infrastructure entity.

According to the merger agreement, all the assets, rights, licenses, agreements, powers and authority of the merging companies are to be conferred on the merged entities, and the merged entities would be liable for all of the obligations of the entities absorbed in the merger, which will be liquidated without dissolution, effective from the date of the completion of the merger.

The holdings of each party to the merger in Gvanim are to be based on the number of each party s cable television subscribers as of August 31, 2002 and Internet subscribers as of November 30, 2002. Following completion of the merger, it is anticipated that we will hold approximately 26% of the issued share capital of the merged broadcasting entity. The possibility that we will increase our proportionate holding in the merged entity is being considered in the context of the merger negotiations.

Under the merger agreement obligations will be attributed to each party to the merger, which shall reflect, per each party s subscriber as of December 31, 2001, equal debt, in an amount that shall be determined by the parties to the merger. Upon completion of the merger, the parties will settle the difference between the obligations attributed to each party and the actual debt per subscriber, as reflected in the financial statements of each party as of December 31, 2001, as transferred to the merged entity.

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In accordance with the merger agreement, the designated shareholders of the merged entity will enter into a certain shareholders agreement within the framework of the merger, effective as of the date of the completion of the merger. The merger agreement and the agreed upon version of the shareholders agreement are subject to their signing by all the parties to the agreements. The parties have agreed that if the final version of the merger agreement has not been signed by July 31, 2003, unless otherwise agreed upon by the parties, the parties shall not have a claim or suit towards another party with respect to the proposed merger agreement and/or the shareholders agreement.

In accordance with the merger agreement, upon receipt of the required approvals, the merger will be effected automatically, effective as of December 31, 2001. Prior to the merger we will need to reach an understanding with the major Israeli banks, which are creditors of the parties to the merger. The merger must also receive approvals under applicable law, including the approvals of the Council, the Income Tax Commission, and the Controller of Restrictive Business Practices and by the Israeli court, after receiving the approvals of certain creditors and the relevant corporate bodies of the relevant parties. To date, approvals have been granted, subject to terms and conditions, from the Council, the Controller of Restrictive Business Practices and the Income Tax Commission. Subject to the final terms of the merger, further approval of the Income Tax Commission to the merger may be required. One of the issues outstanding to date in connection with the consummation of the merger is regarding the position of the Supervisor of the Banks of the Bank of Israel in connection, among other things, with the matter of certain limitations under Israeli banking laws.

One of the other Israeli cable television operators, Tevel Israel International Ltd., filed a motion for stay of proceedings on April 22, 2002. The stay of proceedings was granted by the Court on April 23, 2002, and is currently valid until July 2, 2003. The legal implication of the stay of proceedings is that it is not possible for a claim to be brought against Tevel during the period of the stay, and all past debt incurred by Tevel prior to April 22, 2002, shall be dealt with in accordance with a creditors arrangement to be proposed by the court appointed Trustee, who is also responsible for the management of Tevel during the period of the stay. The approval of the Court is required in order for Tevel to participate as a party to the merger. The current financial situation of Tevel and any possible future deterioration of Tevel may affect the possibility of the consummation of the merger between the Israeli cable television operators, and the conditions that the creditors of the companies that are parties to the merger may impose.

Subject to regulatory approvals, the completion of the merger will enable the merged company to provide additional telecommunication services.

As of April 2002, in accordance with the approval of the Controller of Restrictive Business Practices to the proposed merger, we cooperate with the other two Israeli cable television operators, among other things, in our marketing activities and entire content activities.

The Approval of The Council for Cable and Satellite Broadcasting

The approval of the Council to the merger of March 7, 2002, as amended on February 13, 2003, is subject to a number of conditions, including:

an obligation upon the cable television operators to allow direct broadcasting by YES, to broadcast channels 3, 4, 5 & 6 (family, movies, sport and children, respectively), for consideration. This obligation expires upon the earlier of either: December 31, 2003 (regarding the family, movie and sports channels), and March 1, 2003 (regarding the children s channel); or the date on which YES has at least 500,000 subscribers, after which YES may request an extension. The obligation regarding the children s channel has since expired, however YES has purchased the rights to broadcast the children s channel directly from its producer;

an obligation of unbundling , obliging the merged entity to grant special broadcast license holders which broadcast on a digital platform a non-exclusive permit, for consideration, to use its network in order to transfer their broadcasts (which will be up to a maximum of the higher of either: (i) one sixth of our broadcasting network capacity; or (ii) 75 Mhz from the date of the approval of the merger, including the capacity required for dedicated channels and special cable broadcasting licensees (one sixth of the broadcasting network capacity); and 150Mhz after 2005);

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a maximum subscriber fee for the basic packages (digital or analog) of NIS 156 incl. VAT, linked to the combined index, that includes the Israeli consumer price index of December 2001 (published January 15, 2002) and the US dollar exchange rate as published by the Bank of Israel, or any other index as shall be determined in regulations. The effectiveness of the Council s approval regarding the said linkage to the combined index is subject to the amendment of the applicable regulations promulgated under the Telecommunications Law. To date, the Ministry has not adopted such an amendment;

an obligation to sell 20% of the entity that shall control broadcasting content (as opposed to infrastructure) to third parties, within four years from the date of the decision (in relation to which a public offering will be considered such a sale) unless certain conditions stipulated in the decision shall occur;

a limitation upon the number of channels which the cable television operators shall be allowed to produce (not including up to 16 optional channels on a pay-per-view and near video on demand basis); and

the provision by all of the cable television operators of a guarantee of NIS 45 million to cover the obligations of the merged entity under the Council s approval, and all the Cable Broadcast Licensees (taking into account any amount already provided by way of guarantee pursuant to all the Cable Broadcast Licenses). Our pro rata portion of the NIS 45 million amounts to approximately NIS 11 million.

In addition, in accordance with the approval of the Council, in the event that the Council is convinced that there is a material regression in competition in the multi channel television market, the Council is entitled to instruct the cable television operators to allow each special and general cable broadcast license holder, that broadcasts in a digital format, use of our infrastructure in order to access all potential subscribers, even if they are not our subscribers, so long as our cable network infrastructure reaches their premises. According to the Council s decision, a material regression will be deemed to occur, among other things, in the event that YES shall cease its operation or the merged entity shall provide services to more than 80% of multi-channel television subscribers in Israel.

Pursuant to the Council s amended approval, an application for a general broadcast license was filed with the Council on behalf of the merged entity on March 5, 2003.

In accordance with Council s approvals to the merger, upon the merger, the terms of the Council s approvals to the merger will be an integral part of the terms of the Cable Broadcast License of the cable television operator or any merged entity in place of the cable television operators.

The eventual application of the above terms and other provisions are subject to interpretation and clarification.

The Approval of the Controller of Restrictive Business Practices to the Merger

The approval of the Controller of Restrictive Practices to the merger, granted in April 2002, is also subject to a number of terms and conditions, set forth below. On April 14, 2003, the Controller extended the validity of his approval to the merger until the earlier of June 6, 2003 or the completion of the merger. On June 4, 2003, the Controller extended the validity of his approval to the merger until June 22, 2003, and on June 19, 2003, the Controller further extended the validity of his approval to the merger until the earlier of November 15, 2003 or the completion of the merger. The eventual application of these terms and conditions and the way in which they will work together with the terms of the Council s approval may be subject to interpretation and further clarification.

Separation of activities: the merged entity shall conduct its activities through a broadcasting entity and a cable infrastructure entity, whose activities must be completely separated.

Unbundling: the merged infrastructure entity must allow other cable broadcast license holders to use its cable infrastructure on terms that are not inferior to those offered to the merged broadcasting entity, up to the same maximum commitment as provided by the terms of the approval of the Council, with the additional stipulation of not less than 75 Mhz from the date of the consummation of the merger, and not less than 100Mhz after January 2005 for third parties who are not dedicated channels. This obligation shall not apply to any broadcaster of multi channel national television broadcasts, on a national infrastructure network in its control, unless there is a material regression in the multi channel television market. In the event that the Controller considers there to be a material regression in the multi channel television market for subscribers, he shall have the authority to instruct the merged infrastructure entity (and if necessary, the merged broadcast entity) to provide any cable broadcast license holder the telecommunications infrastructure services needed to supply the package of channels of such licensee to any person whose premises is reached by the cable network (Homes Passed) even if such person is not a subscriber of the merged broadcast entity; however, such instruction shall not oblige the merged infrastructure entity to lay down additional telecommunications infrastructure for such a cable broadcast license holder, to a person who is not a subscriber of the merged broadcast entity. Without derogating from the above, in the event that YES ceases to operate, it will be deemed to be such a material regression in competition. Regarding these conditions, YES or its successor shall be deemed to be such a cable broadcast license holder if it ceases its operation due to insolvency.

Restrictions upon the corporate structure: within 48 months of the Controller s approval, at least 20% of the controlling entities of the merged broadcasting entity must be owned by an entity that does not hold, directly or indirectly, any means of control in any other cable or infrastructure entity. This restriction may be amended or waived at the discretion of the Controller, or will be deemed inapplicable, if either at the end of 48 months there are at least two other holders of a general cable broadcasting license in Israel that are not linked to either the merged broadcasting entity or the merged infrastructure entity; or, if the Minister of Communications has set rates for usage of the merged entity s infrastructure by third parties within 30 months of the date of the approval (and the Controller approves that such rates encourage competition significantly*)*. According to clarifications provided by the Controller in relation to this obligation, in the event that 20% of the means of control of the merged infrastructure entity is purchased by a third party and 20% of the means of control of the merged broadcast entity is purchased by a different third party, neither of whom have a connection to the existing cable television operators, it will not be necessary to meet this requirement.

Restrictions upon the ownership and purchase of broadcasting material:

(i) The merged broadcasting entity and the merged infrastructure entity shall be prohibited from holding means of control of a producer of a channel, except the family channel (Channel 3) and the movie channel (Channel 4) in the basic packages, and shall be prohibited from owning or having any interest in any other producer of a channel, unless it has received authorization to the contrary from the Controller by way of amendment of the terms of the Controller s approval to the merger. A producer of a channel means a producer of a channel that at least 20% of its content expenses or its hourly broadcasts are derived from content that was purchased or packaged in Israel. Subsequent to the approval and pursuant to the said restriction, we sold and transferred options that we held to purchase certain interests in the Hop channel, the sports channels (Channel 5 and the Sport 5+ channel), the children s channel (Channel 6) and the culture and science channel (Channel 8).

(ii) The merged broadcasting entity and the merged infrastructure entity is permitted to use the content of another producer, but shall be prohibited from owning the content of anther producer, and further, these entities shall be prohibited from determining to whom content shall be sold or transferred to third parties for use (with the exception of agreements with the major producer companies, namely Warner Bros., Universal, Buena Vista (Walt Disney), Paramount, MGM, Columbia, and Twentieth Century Fox, which were signed prior to the date of the Controller s merger approval and received prior regulatory approvals).

(iii) The merged broadcasting entity shall only be allowed to purchase content for the family and movie channels and for Pay-Per-View and Near Video On Demand, and such purchase shall be in accordance with restrictions concerning, among other things, the purchase of exclusive content. In addition, the merged broadcasting entity shall have a must sell requirement to YES or any other general license holder regarding certain material content broadcast on the family and movie channels (Channel 3 and 4, respectively) stipulated in the Controller s approval. Further, all content purchased, by any party to the merger or any person related to such parties, from the major producer companies within 24 months following the Controller s approval to the merger, shall be subject to the must sell requirement to YES or any other general license holder, provided that any person who receives content pursuant to this must sell requirement shall also be subject to the must sell requirement with respect to contents purchased or that may be purchased from the major producer companies during such period.

*Obligation to supply multi channel television broadcasts to the entire population of Israel:*subject to price restrictions, and existence of appropriate infrastructure.

Infrastructure:

The merged infrastructure entity shall be prohibited from preventing the development of competing infrastructures, and shall be prohibited from using its control over the merged infrastructure to prevent or hinder competition. Unless prior written consent has been received from the Controller, both the merged broadcasting entity and the merged infrastructure entity shall be prohibited from holding any interest, directly or indirectly, in any person or entity that holds an interest greater than 10% in any other company that owns infrastructure for cable television or any other infrastructure for telecommunications services.

The merged infrastructure entity shall be prohibited from preventing any registered building contractor from laying down infrastructure, regardless of the presence of infrastructure belonging to the merged entity already in such area. Without derogating from the above, the infrastructure entity shall be prohibited from preventing a building contractor from laying down infrastructure in places where it has laid its own infrastructure, subject to the receipt of an indemnity for any damages to its infrastructure caused thereby.

The merged infrastructure entity and the merged broadcasting entity shall be separated entirely from Internet service providers. In addition, companies such as Barak I.T.C. (1995) The International Telecommunications Services Corp. Ltd., and other Internet service providers connected to the cable television operators or their shareholders, are also prohibited from transferring Internet service provider activities to the merged entities.

The merged infrastructure entity and the merged broadcasting entity shall be prohibited from preventing any end user which has Inside Wiring on his property from: (i) connecting with any other provider of multi channel television; (ii) the common use of Inside Wiring by such user to connect to another provider in addition to the merged entities; and (iii) access by such end user to Internet infrastructure, or access by such end user to Internet services, which are marketed either by the merged infrastructure entity or by the merged broadcasting entity, even in the event that such end user purchases multi channel television from a competitor. The merged entities shall still be subject to the administration directives published by the Minister of Communications governing the reciprocal obligation to lease Inside Wiring between the cable television operators and YES.

Restrictions upon connected persons or entities:

The terms of the Controller s approval shall equally apply to any person or entity connected to the cable television operators, the infrastructure entity, or the broadcast entity whose action is needed in order to fully and exactly comply with all or part of such terms. Any restriction or condition applying under the terms of the Controller s approval upon a party to the merger, on the infrastructure entity, or on the broadcast entity, shall also equally apply to any person or entity connected to them, and non compliance with such restriction or condition by a connected person or entity, or together with such connected person or entity, shall be deemed to be non compliance with the terms of the Controllers approval on the part of the party to the merger to which such person is connected, and by non compliance by the broadcast entity and the infrastructure entity to which such person or entity is connected.

Restrictions shall also apply upon the activities of the officers or owners of the groups of the controlling shareholders of the merged entities, including, among others, as follows:

prohibition upon such officers having activities in businesses that compete, directly or indirectly, with the business of the merged broadcasting entity and/or the merged infrastructure entity, without the written approval of the Controller of Restrictive Business Practices;

prohibition upon such owners from sharing information related to the business of the merged broadcasting entity and/or the merged infrastructure entity;

an enforced total separation between specific named Israeli corporate entities such as cell phone telecommunications companies and newspapers, on the one hand, and the merged broadcasting entity and the merged infrastructure entity, on the other hand.

If the merged broadcasting entity shall be allowed to air commercials in multi channel television channels, then the Controller of Restrictive Business Practices shall have the authority to impose further restrictions stemming from concerns arising from the cross interests of the controlling shareholders of the parties to the merger in other entities that sell commercial time to the public.

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*Interests in telephony services:*the merger shall be conditional upon the fact that the merged entity shall supply domestic fixed line telephony services on cable infrastructure in accordance with:

the merged infrastructure entity is required to file an applications for a license for the provision of fixed line telephony services by the merged infrastructure entity within 3 months of the date of the Commissioner s approval; and

a minimal infrastructure investment commitment of not less than NIS 350 million, to be completed in stages as follows: NIS 105 million until 31 December 2003, NIS 140 million in 2004 and NIS 105 million in 2005; and

a condition that the merged entities will begin to provide domestic fixed line telephony services over cable infrastructure to the Israeli public within a year of receipt of its infrastructure license and no later than two years from the date of the Controller s approval to the merger. Such obligation relates to any residential area comprising at least 10,000 residents in 15 so called separate geographical areas ; and

obligatory milestones as to the number of business and residential customers that the telephony company must obtain for each year.

In accordance with the terms of the approval of the Controller of Restrictive Business Practices to the merger, in July 2002, the Israeli cable television operators through Telecom Gold 2001 & Co. (a limited partnership) filed an application for the merged infrastructure entity for an infrastructure license, which includes the provision of fixed line telephony services. To date, this license has not yet been granted.

Bank Guarantee: the approval of the Controller of Restrictive Business Practices to the merger is also conditional upon the provision of a bank guarantee in the amount of US $15 million to ensure compliance with the terms of the approval of the Controller. In the event that the Controller of Restrictive Business Practices decides, in his discretion, that there has been a material breach of the terms of the approval, he may fully exercise the guarantee. We have provided our pro rata portion of this guarantee in the amount of $3.75 million.

In the event of a non-material breach, the Controller may exercise $500,000 of the bank guarantee in relation to each breach, and an additional $500,000 per month, until such breach is remedied. Such amounts are non refundable and the guarantee must be maintained at US$15 million at all times, including in the event of breach. The provision and usage of the guarantee does not derogate from the Controller s ability to take any other remedy according to the provisions of the Restrictive Trade Practices Law against the merged entities in the event of breach.

There can be no assurance that the merger will be consummated, and if consummated: (i) whether the conditions of the merger will enable the merged entity to successfully compete; or (ii) whether there will be a successful integration between the merging entities, or (iii) whether the combined entity will be able to compete effectively against current or future competitors and realize the anticipated benefits of the merger.

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4C. ORGANIZATIONAL STRUCTURE

We have six significant subsidiaries, all of which are Israeli companies, which we control directly or indirectly, as described below.

Matav Investments Ltd. Matav Investments Ltd. is wholly owned by us and it owns 100% of the share capital of Matav Assets Ltd. Through Matav Investments Ltd. we are the beneficial owners of 10% of the share capital of Barak I.T.C. (1995) The International Telecommunications Services Corp. Ltd., an international telephony service provider in Israel, and through Matav Investments Ltd., we are the beneficial owners of approximately 7.42% of the share capital of Partner Communications Company Ltd., the third of four licensed providers of mobile cellular telephone services in Israel, and one of the two operators which use GSM. Until April 2002, through Matav Investments Ltd. we were the beneficial owners of approximately 15.2% of Partner, at which time we sold approximately half of our shares in Partner.

Cable Systems Media Haifa-Hadera Ltd. Cable Systems Media Haifa-Hadera Ltd. is wholly owned by us, and holds the Cable Broadcast License for the Haifa-Hadera area.

Matav Infrastructure 2001 L.P., of which we own approximately 72% of the rights, with the remainder being held by our wholly owned subsidiary cable systems Media Haifa-Hadera Ltd. Matav Infrastructure 2001 L.P. holds the infrastructure license.

Matav Assets Ltd. Matav Assets Ltd. is wholly owned by us, through Matav Investments Ltd., and engages in real estate activities.

Matav Infrastructure Ltd. is wholly owned by us, and is the general partner of Matav Infrastructure 2001 L.P.

Nonstop Ventures Ltd., of which we hold 50% of the issued share capital, with the remainder being held by several of our shareholders.

We are part of the Dankner Group, and Dankner Investments Ltd. is our controlling shareholder. As at June 20, 2003, Dankner Investments Ltd. holds approximately 47.74% of our outstanding ordinary shares and 49.70% of the voting rights. The difference between the shareholdings and the voting rights derives from the fact that at as June 20, 2003, a fully owned subsidiary holds ordinary shares representing approximately 3.95% of our outstanding share capital, which do not grant voting rights under the Israeli Companies Law for so long as such shares are held by Cable Systems Media Haifa-Hadera Ltd. Pursuant to a shareholders agreement, it has caused the nomination of the majority of the members of our board of directors. For additional information regarding the shareholders agreement, see Item 7. Major Shareholders and Related Party Transactions . The shares of Dankner Investments Ltd. are publicly traded on the Tel Aviv Stock Exchange.

The Dankner Group was established in 1957 and is today one of Israel s leading privately owned concerns with diversified interests in banking, communications, real estate, as well as manufacturing of salt, petrochemicals and plastics.

The banking division of the Dankner Group is through its control of Israel Salt Industries Ltd., a public company traded on the Tel Aviv Stock Exchange, which is the owner of 11.63% of Bank Hapoalim Ltd., the largest bank in Israel. Israel Salt Industries are part of the controlling group of Bank Hopoalim, which constitutes approximately 45.18% of the Bank. Pursuant to an agreement of February 2003, Israel Salt Industries Ltd. shall sell, subject to certain conditions, part of its shares in Bank Hapoalim Ltd., which constitute up to approximately 1.93% of the issued share capital of the Bank, to Gandan Holdings Ltd. (whose major shareholders are individuals of the Dankner family). The shares of Bank Hapoalim are publicly traded on the Tel-Aviv Stock Exchange.

The communication division of the Dankner Group is materially comprised of its holdings of our shares and, through us, its indirect holdings in Partner Communications Company Ltd. and Barak I.T.C. (1995) The International Telecommunications Services Corp. Ltd.

The real estate division of the Dankner Group is located under Dankner Investments Ltd., which is one of the leading real estate companies in Israel. Dankner Investments Ltd. specializes in integrated residential neighborhoods and shopping centers. Together with its joint venture partners, Dankner Investments Ltd. develops thousands of housing units throughout Israel.

The salt division of the Dankner Group is operated by Israel Salt Industries Ltd., which operates highly mechanized solar evaporation plants that produce pure, high quality industrial and edible salts. Plants are located at Atlit on the Mediterranean, Kalia and Sodom on the Dead Sea and Eilat on the Red Sea. Over 25% of the annual production of Israeli Salt Industries Ltd. is exported to the Far East, Africa and Europe. In addition to its salt manufacturing activities, Israeli Salt Industries Ltd. specializes in marine agriculture and water treatment.

The chemical and plastic divisions of the Dankner Group are operated by Dor Chemicals Ltd., a public company traded on the Tel Aviv Stock Exchange, specializing, directly and indirectly through its subsidiaries, collectively known as the Dor Chemicals Group, in the production and marketing of raw materials in the chemical and plastic industries. In addition, the Dor Chemicals Group hold certain rights in marine licenses to search for natural gas along the coasts of Israel and in a consortium that won a tender for the desalination of sea water.

In the plastic division, the Dor Chemicals Group, directly and through its subsidiaries in Italy and Belgium (Moplefan S.p.A and its subsidiaries), in Australia (SHORKO AUSTRALIA PTY LTD.) and in Germany, France, South Africa and Mexico (Trespaphan GmbH and its subsidiaries), engages in the manufacture and marketing of biaxial-oriented polypropylene and case polypropylene film of different types. The products are used for packaging and wrapping materials in the tobacco, textile, food, medical equipment and adhesive band industries.

In the chemical division, the Dor Chemicals Group engages in the manufacture and marketing of intermediate materials for the gasoline, chemicals, plastics, pharmaceuticals and wood industries. The product range includes MTBE (a high-octane gasoline component), hydrogen, formaldehyde, para-formaldehyde and Fodor (disinfectant formulation for agricultural use). The chemical division of the Dor Chemicals Group also imports and markets methanol as a raw material, for the manufacture of some of its own products and to supply to its costumers.

The chemical division of the Dankner Group is also operated by Carmel Chemicals Ltd., with its subsidiaries Carmel Resins Ltd.and Alex Control Systems Ltd., which manufactures thermosetting, melamine and urea-molding compounds used to manufacture tableware, sanitary-ware, electrical accessories, closures and the raw materials for plastic media blast, or PMB. Other products are resins and adhesives for the wood, timber, paint, paper carton and textile industries, casting compounds in a wide spectrum of patterns and colors for making decorative marble with granite-like texture, used for the production of sanitary-ware and tabletops. Most of the output of the Carmel companies is exported to North America, Europe and the Far East.

Currently, the Dankner Group is in the process of structural reorganization, in connection with which, among other things, Elran (D.D.) Investments Ltd., or Elran , a public company traded on the Tel Aviv Stock Exchange, entered into a series of agreements for the purchase of shares of Dankner Investments Ltd. from various members of the Dankner family, at a price per share of approximately $4.2, which shall constitute, in the aggregate, approximately 53.63% of the outstanding share capital of Dankner Investments Ltd. as of February 27, 2003. Under these agreements, upon the occurrence of certain circumstances, the number of shares to be purchased by Elran may change, so long as the number of shares shall not, in the aggregate, constitute less than 50.01%, or exceed approximately 61.26%, of the outstanding share capital of Dankner Investments Ltd. following the purchase. The effectiveness of these agreements is subject to the fulfillment of certain conditions, among others, regulatory conditions under our Licenses, including the receipt of the approval of the Minister, the Council and the General Manager of the Ministry of Communications to the indirect transfer of the means of control of Matav. We applied to these communication authorities for the required approvals. On May 1, 2003, we received the approval of the Council, which is subject to certain conditions, on June 2, 2003, we received the approval of the Minister and on June 11, 2003 we received the approval of the General Manager of the Ministry of Communications. To date, some conditions precedent of these agreements are still outstanding.

4D. Property, Plants and Equipment

We own our telecommunications network infrastructure and related equipment. Our network infrastructure includes 458,002 Homes Passed in the length of approximately 6,042 km. See Item 4B Technological Preparations for Competition in the Telecommunications Market .

Our principal executive offices are in Netanya, Israel in a building purchased by us in 1992 for approximately NIS 3.0 million, which currently has 1,528 square meters of built space.

Our HeadEnd, studio and regional administrative offices in Haifa are situated in a 1,700 square meter building on 6,690 square meters of land leased from the Israel Lands Authority pursuant to a lease which will expire in 2040. In July 1991, we paid approximately NIS 1.5 million, constituting the entire amount due under such lease in advance as well as approximately NIS 3.8 million to the City of Haifa for the buildings on the plot. We have an option to renew the lease for 49 additional years.

Our HeadEnd in Bat-Yam is situated on a 200 square meter property, which we lease under a lease agreement providing for a monthly rent of NIS 10,724. The lease is scheduled to expire in August 2003. We have an option to extend the lease for an additional period of one year.

Our HeadEnd and microwave broadcast tower in Ramot-Naftali is situated on 520 square meters of land, owned by the Israel Lands Authority, which is subleased to us by the Mevot Hermon Local Council under a lease agreement expiring in October 2006, of which 160 square meters is the HeadEnd and 77 square meters is a basement. Pursuant to the terms of the lease agreement, we are obligated to pay the Mevot Hermon Local Council an annual fee of NIS 1 and to provide cable television services to the residents of Moshav Kadesh Naftali free of charge. Upon termination of the lease agreement, our interest in the property will pass to the Mevot Hermon Local Council, although we will be entitled to remove all of our transmission equipment.

We also hold real property in Bat-Yam of 2,500 square meters, under a lease from the Israel Lands Authority which is scheduled to expire in 2038. In 1989, we paid approximately NIS 1.8 million for this lease, constituting the entire amount due under the lease, in advance, and approximately additional NIS 1.28 million in order to extend the deadline under the lease for completion of a building on the property to January 1, 1997. Since negotiations with the relevant authorities concerning the required permits and approvals for the building have failed, we rent this property under a short-term sub-lease and intend to sell it in the future.

In Pardess Hanna, we lease a 1,009 square meter plot of land from the Israel Lands Authority. Two structures which contain a HeadEnd for the Hadera license area are located on this property.

In 1999, we purchased 1,927 square meters in a building near our headquarters in Netanya, for approximately NIS 8.4 million. We use this property, among other things, for our Netanya Hadera cable operations and for our High Speed Internet over cable activities.

In addition to the foregoing, we lease several other small properties totaling approximately 4,000 square meters throughout our operating areas, which we use for office space, storage, and microwave reception towers. Altogether with the leased properties described above, the aggregate monthly rental payments made by the Company are approximately $20,000.

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ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following operating and financial review and prospects are based upon and should be read in conjunction with our financial statements and selected financial data, which appear elsewhere in this annual report. You should also read the risk factors appearing elsewhere in this annual report for a discussion of a number of factors that affect and could affect our financial condition and results of operations.

The financial statements have been prepared in accordance with Israeli GAAP. As applied to our financial statements, Israeli GAAP and U.S. GAAP vary in certain respects, as described in Note 20 to the financial statements. The financial information in this section is presented in adjusted NIS, unless stated otherwise.

We reported certain amounts in adjusted NIS which have been translated for convenience into US dollars using the representative exchange rate of the US dollar as published by the Bank of Israel on December 31, 2002 ($1.00 = NIS 4.737). Except where otherwise stated, amounts appearing in dollars have been translated from NIS at the above exchange rate.

Critical Accounting Policies

In order to improve understanding of the discussions below, it is important to obtain some degree of familiarity with our principal or significant accounting policies. These policies are described in Note 2 to the Consolidated Financial Statements listed in Item 18. We review our financial reporting, disclosure practices and accounting policies annually to ensure that the financial statements developed, in part, on the basis of these accounting policies provide complete, accurate and transparent information concerning the financial condition of our company. As part of this process, we reviewed the selection and application of our critical accounting policies and financial disclosures as of December 31, 2002.

In preparing our financial statements in accordance with generally accepted accounting policies, our management must often make estimates and assumptions which may affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures as of the date of the financial statements and during the reporting period. These estimates and judgments are reviewed by management on an ongoing basis, and by the Audit Committee at the end of each quarter prior to the public release of our financial results. Some of those judgments can be subjective and complex, and consequently actual results may differ from those estimates. For any given individual estimate or assumption made by our management, there may be alternative estimates or assumptions which are also reasonable. We consider our most significant accounting policies to be those relating to depreciation of fixed assets, allowance for doubtful accounts and Contingent liabilities, which are discussed below:

Depreciation of fixed assets:

Our fixed assets are depreciated by the straight-line method on basis of their estimated useful life. A significant portion of our operating expenses results from depreciation of fixed assets. The vast majority of our fixed assets are composed of cable network, equipment in the broadcasting centers and studios and converters. If rapid technological changes are to occur in our industry, the estimated useful life of parts of our fixed assets could be shortened and consequently increase the annual depreciation costs and operating expenses.

Allowance for doubtful accounts:

The allowance is principally determined for specific debts that are doubtful of collection, based on the age of the customers debt. Our revenues are derived from a large number of subscribers in the license areas. We perform ongoing credit evaluations of our subscribers for the purpose of determining the appropriate allowance for doubtful accounts, by taking into account variables such as past experience, age of the receivable balance, and current economic conditions that may affect a subscriber s ability to pay. The use of different estimates or assumptions could produce different allowance balances. We fully provide for the balance of disconnected subscribers. If the financial condition in Israel was to deteriorate, resulting in an impairment of our subscriber s ability to make monthly payments, additional allowance for doubtful accounts may be required. If we were to face stronger competition, we might experience a higher rate of disconnections and hence additional allowance for doubtful accounts may be required.

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Contingent liabilities:

We are a party to certain legal actions as described in Item 8A - Consolidated Statements and Other Financial Information - Legal and Arbitration Proceedings and described in Note 12 in the financial statements.

With regard to claims and petitions for certification of some of these actions as a class actions, we believe, based on the opinion of our legal counsels, that since the claims and petitions for certification of them as class actions, and the Company s response to the claims and petitions, raise complex questions, both legal and factual, which have not yet been resolved in Israeli case law and for which there are no precedents based on similar facts, it is not yet possible to evaluate the claims chances, and therefore, no provision has been included in the Company s financial statements in respect of the said claims. With regard to other claims, in which the proceedings are in early stages, the prospects of the claims cannot be estimated and no provision has been included in the Company s financial statements in respect of such other claims. As to the rest of the other claims, we believe, based on the opinion of our legal counsels, that the Company has good defensive arguments against these claims, and therefore, no provision has been included in the Company s financial statements in respect of the said claims.

As additional information becomes available, we will assess the potential liability related to our pending litigation and revise our estimates if needed. Such revisions in our estimates of the potential liability could materially impact our results of operation and financial position.

New Accounting Standards in the United States

In April 2002, the Financial Accounting Standards Board (or the FASB) issued Statement of Financial Accounting Standard No. 145, Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections (or SFAS No. 145), which rescinds SFAS No. 4, Reporting Gains and Losses from Extinguishment of Debt and an amendment of that Statement, and SFAS No. 64, Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements. SFAS No. 145 also rescinds SFAS No. 44, Accounting for Intangible Assets for Motor Carriers. SFAS No. 145 amends SFAS No. 13, Accounting for Leases, to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions. SFAS No. 145 also amends other existing authoritative pronouncements to make various technical corrections, clarify meanings, or describe their applicability under changed conditions. SFAS No. 145 is effective for fiscal years beginning after May 15, 2002.

In June 2002, the FASB issued Statement of Financial Accounting Standard No. 146, Accounting for Costs Associated with Exit or Disposal Activities (or SFAS No. 146), which addresses significant issues regarding the recognition, measurement, and reporting of costs associated with exit and disposal activities, including restructuring activities. SFAS No. 146 requires that costs associated with exit or disposal activities be recognized when they are incurred rather than at the date of a commitment to an exit or disposal plan. SFAS No. 146 is effective for all exit or disposal activities initiated after December 31, 2002.

In November 2002, the FASB issued FASB Interpretation No. 45, Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an interpretation of FASB Statements No. 5, 57, and 107 and Rescission of FASB Interpretation No. 34 (or FIN No. 45). FIN No. 45 elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. FIN No. 45 does not prescribe a specific approach for subsequently measuring the guarantor s recognized liability over the term of the related guarantee. It also incorporates, without change, the guidance in FASB Interpretation No. 34, Disclosure of Indirect Guarantees of Indebtedness of Others, which is being superseded. The disclosure provisions of FIN No. 45 are effective for financial statements of interim or annual periods that end after December 15, 2002, and the provisions for initial recognition and measurement are effective on a prospective basis for guarantees that are issued or modified after December 31, 2002, irrespective of a guarantor s year-end.

We do not expect the adoption of the abovementioned standards to have a material impact on our results of operations or financial position.

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New Accounting Standards in Israel

During October 2001, the Israel Accounting Standards Board published Accounting Standard No. 12 with respect to the discontinuation of the adjustment of financial statements, and Accounting Standard No. 13 with respect to the effect of the changes in the exchange rates for foreign currencies. In August 2002, Accounting Standard No. 14 was published with respect to fiscal reporting for interim periods, and in December 2002, Accounting Standard No. 17 was published with respect to the deferral of the implementation of Accounting Standards No. 12 and No. 13 until January 1, 2004. In February 2003, Accounting Standard No. 15 was published with respect to the impairment of assets.

According to Standards No. 12 and No. 17, which deal with the discontinued adjustment of financial statements, financial statements will discontinue to be adjusted for inflation in Israel commencing January 1, 2004. Until December 31, 2003, we will continue to prepare adjusted financial statements in conformity with Opinion No. 36 of the Institute of Certified Public Accountants in Israel. The adjusted amounts included in the financial statements as of December 31, 2003, will serve as the starting point for nominal financial reporting beginning January 1, 2004.

The provisions of Accounting Standard No. 13 and No. 17 prescribe principles with respect to the effect of the changes in the exchange rates for foreign currency. These Standards replace clarification No. 8 and clarification No. 9 to Opinion No. 36 of the Institute of Certified Public Accountants in Israel, which are void with the discontinuation of the adjustment of financial statements. The Standards deal with the translation of transactions in foreign currency and the translation of financial statements of foreign operations in order to integrate them into the financial statements of the reporting company. The translation principles of Accounting Standard No. 13 are different from those implemented to date. Accounting Standard No. 13 will apply to financial statements for periods commencing after December 31, 2003.

The objective of Accounting Standard No. 14, which deals with fiscal reporting for interim periods, is to determine the minimum content for financial reporting for interim periods, as well as to determine the recognition and measurement principles in financial statements for interim periods. In addition, the interim financial statements will, for the first time, include condensed segmental information similar to the information included in the annual financial statements. This Accounting Standard, which is based on International Accounting Standard No. 34, Financial Reporting for Interim Periods , replaces Opinion No. 43 of the Institute of Certified Public Accountants in Israel that deals with financial statements for interim periods and Opinion No. 60 that deals with the amendment of Opinion No. 43 with respect to the cancellation of the obligation to include information regarding nominal data in financial statements for interim periods. This Standard will apply in respect to financial statements for periods beginning on or after January 1, 2003.

Accounting Standard No. 15, which deals with the impairment of assets, is based on International Accounting Standard No. 36, and prescribes the accounting principles in the case of a decline/elimination of the decline, in the value of a company s assets, including investments in investees that are not subsidiaries, goodwill arising from the acquisition of subsidiaries and fair value adjustments. This Standard will apply with respect to financial statements for periods commencing on or after January 1, 2003.

The transitional guidelines in the Standard prescribe that losses due to an impairment of assets, which derive from the application of this Accounting Standard, will be recognized in the pre-tax income. The aforesaid will not apply in the case of a loss from the impairment of an asset that was not recognized in the past only due to the fact that the total undiscounted expected future net cash flow exceeds the book value. The latter will be carried to the statement of operations under the item Cumulative effect of the change in the accounting principle to the beginning of the year .

We do not anticipate that the new Standards (not including standard No. 12), as discussed above, will have a significant effect on our results of operations, financial position and cash flows.

As for standard No. 12, we anticipate that it will have a significant effect, in a positive inflationary environment, on our operations, financial position and cash flows.

5A. Operating Results

We were formed in June 1987. We began building out our cable television network and offering cable television services on a trial basis in November 1989. In March 1990, we began providing full cable television services. Between 1990 2002, we operated pursuant to five exclusive franchises granted to us by the Ministry of Communications for Bat-Yam and Kiryat Shemona Holon, Safed and the Golan Heights, Haifa and Hadera, and Netanya and the Sea of Galilee. During 2002, these franchises were replaced by two general non-exclusive Cable Broadcast Licenses, a Telecommunications Infrastructure License and a Broadcasting HeadEnd License. Under the terms of our previous franchises and current licenses, we pay the Ministry of Communications variable and fixed franchise/license royalties. For the years ended December 31, 2000, 2001and 2002, we paid royalties of NIS 23.8 million, NIS 22.4 million and NIS 21.0 million, respectively.

As of December 31, 2002, we provided cable television services to 274,884 subscribers, representing approximately 26% of all cable television subscribers in Israel, and have achieved an average subscriber penetration rate of approximately 60% for all of our license areas. For the years ended December 31, 2000, 2001 and 2002, we generated revenue of NIS 483.8 million, NIS 478.4 million and NIS 505.0 million, respectively. Our operating loss for the years ending December 31, 2000, 2001 and 2002, was NIS 62.8 million, NIS 132.3 million and NIS 100.6 million, respectively.

Our net loss for the years ended December 2000 and 2001 was NIS 228.0 million and NIS 262.2million, respectively, and our net income for the year ended December 31, 2002, was NIS 34.5 million. During the years 2000, 2001 and 2002, we achieved EBITDA (Earnings Before Interest, Taxation, Depreciation and Amortization) of NIS 45.4 million, NIS 0.3 million and NIS 57.8 million, respectively. The EBITDA excludes other income or expenses .

Through December 31, 2002, we invested approximately NIS 2,025 million ($427.5 million) in building out our cable television network and in other fixed assets within our license areas. As of December 31, 2002, our cable television network extended 3,755 miles and passed approximately 458,000 homes, or approximately 93% of the households the areas in which we operate.

With our transition to digital cable television services, we increased our revenues but also increased our expenses and investment in digital set top boxes, program content and other services to our subscribers. Each digital set-up box costs us approximately $165. Due to marketing considerations, we do not charge the customer the full cost of the digital set-up box, and we subsidize this cost. We collect a deposit of approximately NIS 254 plus VAT for each such digital set-top box. We have already purchased approximately 210,000 digital set top boxes, including 6000 one-way only set-top boxes. As of May 31, 2003, approximately 56% of our subscribers were equipped with digital set-top boxes.

Revenues

We derive a substantial amount of our revenue from a monthly subscriber fee of approximately NIS 144 plus VAT for providing the analog and the digital Basic Packages of cable television services. We also charge our subscribers a one-time deposit of approximately NIS 84 plus VAT, for the regular analog set-top box (for those subscribers without cable-ready televisions), or NIS 169 plus VAT, for the addressable analog set-top box and NIS 254 plus VAT, for the digital set-top box. We partially refund these deposits when the set-top boxes are returned. The refund amount, linked to the Israeli consumer price index, is reduced to reflect a 10% annual depreciation, for each year or portion of a year in which the subscriber used the set-top boxes. Such depreciation is included in our revenue, exclusive of value added tax. In accordance with an amendment to regulations promulgated under the Telecommunications approved by the Economic Committee of the Israeli parliament on June 16, 2003, the deduction from the deposit for the set-top box is 10% of the value of the set-top box. Alternatively, our subscribers may elect to lease the set-top box for a monthly fee that ranges between NIS 10 and NIS 15 including VAT. Additional revenues are derived from our tiering services, Pay-Per-View services, interactive services, access to High Speed Internet over cable services and other services.

Our revenue per subscriber, penetration rate and churn rate may vary in the future from historical levels depending upon numerous factors, which are mostly beyond our control. These factors include amongst others, the nature of our future cable television and telecommunications services, and the development of competition for revenue per subscriber and the success of our marketing strategies as well as market acceptance of the Company s services by subscribers.

Cost of Revenues and Other Operating Expenses

Our principal operating expenditures are:

- programming costs;
- depreciation and amortization of fixed assets;
- pay-roll and related expenses;
- license (previously franchise) royalties and payments to the government of Israel; and
- maintenance.

Churn

Churn refers to subscriber disconnection from network services, either involuntary, due to non-payment of bills or suspected fraudulent use, or voluntary, due to subscribers terminating their use of our services.

We recognize that managing subscriber churn is an important factor in maximizing revenue and cash flow. In order to control churn caused by subscribers voluntarily terminating our service, we attempt to ensure that our service is high quality and competitive. We use our advanced information technology systems as a tool to understand, monitor and control voluntary churn. We have a retention team within our customer services group that makes follow-up phone-calls to subscribers who call us with complaints or problems in order to resolve any problems and to retain the subscribers on the network. We also host exclusive subscriber events, such as shows and parties for subscribers, in order to encourage subscriber loyalty. For the year ended December 31, 2002, our churn rate for our four operating areas averaged approximately 26%.

Year Ended December 31, 2002 compared with Year Ended December 31, 2001

The following table sets forth for the year 2002 our consolidated statement of operation according to our various business segments:

	Adjusted new Israeli shekels in millions		
	Cable TV	**Internet**	**Total**
Revenue	495.7	9.3	505.0
Operating expenses	504.2	12.9	517.1
Gross loss	(8.5)	(3.6)	(12.1)
Selling and Marketing expenses	38.2	3.2	41.4
General and Administrative expenses	46.0	1.0	47.0
Operating loss	(92.7)	(7.8)	(100.5)
Financial expenses, net	49.0		49.0
Loss after Financial expenses	(141.7)	(7.8)	(149.5)
Other income, net			283.8
Income (loss) before taxes on income	(141.7)	(7.8)	134.3
Taxes on income			110.9
Income (loss) from operation of the Company and its subsidiaries	(141.7)	(7.8)	23.4
Equity in earnings (losses) of affiliated companies, net	11.1		11.1
Net income (loss)	(130.6)	(7.8)	34.5
EBITDA	59.7	(1.9)	57.8

As of January 2000, we introduced a new Internet business as an Internet service provider, which was subsequently discontinued in July 2001 and was a significant cause of losses in the year 2000. The termination of this activity in July 2001 eliminates losses that were attributable to this activity. As of April 2002, following the receipt of our Telecommunications Infrastructure License, we began to provide access to High Speed Internet over cable services on a commercial basis through Matav Infrastructure 2001, LP, a wholly owned limited partnership of Matav Infrastructure Ltd. The comparative discussion below presents total activities, and cable only activities as a percentage of such total activities, and (with the exception of cash flow) compares cable only activities in 2002 with cable only activities in 2001.

Revenue. Total Revenue increased by NIS 26.6 million, or 5.6%, from NIS 478.4 million in 2001 to NIS 505.0 million in 2002. Of the total revenue, approximately 98.2% can be attributed to cable only activities in 2002, in comparison to 98.8% in 2001. Our revenue from cable activities increased by NIS 23 million, or 4.9% from NIS 472.7 million in 2001 to NIS 495.7 million in 2002. Approximately 97% out of our revenue from cable activities in the year 2002 derived from monthly subscription fee, the rest from depreciation of subscribers deposits for set-top boxes, from installation fees, Pay-Per-View services and payments from the Shopping Channel. The increased total revenues, despite a decrease in total subscribers, are attributed to higher sales of tiering and high-speed Internet services.

Operating expenses. Total operating expenses increased by NIS 23.6 million, or 4.8%, from NIS 493.5 million in 2001 to NIS 517.1 million in 2002. Of the total operating expenses, approximately 97.5% can be attributed to cable only activities in 2002, in comparison to 95% in 2001. As a percentage of revenue from cable only activities, operating expenses from cable only activities increased from 99.5% in 2001 to 101.7% in 2002. Our operating expenses from cable only activities (excluding depreciation and amortization of fixed assets) increased by NIS 13.7 million, or 4.1%, from NIS 331.4 million in 2001, to NIS 345.1 million in 2002. As a percentage of revenue from cable only activities, operating from cable only activities (excluding depreciation and amortization of fixed assets) decreased from 70.1% in 2001 to 69.6% in 2002. The increase in operating expenses is mainly derived from an increase in programming costs and depreciation costs due to our investments in infrastructure and digital set-top boxes, as set forth below.

Cable television programming expenses increased by NIS 19.2 million, or 8.4 %, from NIS 228.3 million in 2001, to NIS 247.5 million in 2002. Our cable television programming expenses increased from 48.3% of our total revenue in 2001, to 49.9% in 2002. The increase in programming expenses reflects an increase in tiering services, which generates additional expenses as a result of additional purchase of content. Since all of our programming expenses are either paid in US dollars or linked to US dollars, any substantial devaluation of the shekel against the US dollar will increase the shekel cost of our US dollar denominated expenses.

Depreciation and amortization of fixed assets increased by NIS 20.1 million or 14.5%, from NIS 139.0 million in 2001, to NIS 159.1million in 2002. The increase in depreciation and amortization of fixed assets reflects the continuation of investment in infrastructure and digital set-top boxes.

Other operating expenses from cable activities decreased by NIS 5.4 million, or 5.5%, from NIS 103.1 million in 2001, to NIS 97.7 million in 2002. The decrease in other operating expenses is primarily due to the decrease in salaries.

Selling and marketing expenses. Total selling and marketing expenses decreased by NIS 17.7 million, or 30% from NIS 59.1 million in 2001, to NIS 41.4 million in 2002. Of the total selling and marketing expenses, approximately 92.3% can be attributed to cable only activities in 2002, in comparison to 95% in 2001. Our selling and marketing expenses for cable activities decreased by NIS 17.9 million or 31.0%, from NIS 56.1 million in 2001, to NIS 38.2 million in 2002. As a percentage of total revenue from cable only activities, our selling and marketing expenses decreased from 11.9% in 2001, to 7.7% in 2002. This decrease is mainly due to lower marketing expenses due to a joint advertising campaign of the three Israeli cable television operators. We do not expect sales and marketing expenses to decrease significantly in the future at such a rate, if at all, and may increase.

General and administrative expenses. Total general and administrative expenses decreased by NIS 11.1 million or 19.1% from NIS 58.1 million in 2001, to NIS 47 million in 2002. Of the total general and administrative expenses, approximately 97.9% can be attributed to cable only activities in 2002, in comparison to 91.2% in 2001. Our general and administrative expenses for cable activities decreased by NIS 7 million or 13.2%, from NIS 53 million in 2001, to NIS 46 million in 2002. As a percentage of total revenue, our general and administrative expenses from cable activities decreased from 11.2 % in 2001 to 9.3% in 2002. We cannot assure you that the general and administrative expenses will continue to decrease at such a rate in the future, if at all.

Operating loss and EBITDA. Total operating loss decreased by NIS 31.8 million or 24.0% from NIS 132.3 million in 2001, to NIS 100.5 million in 2002. Of the total operating loss, approximately 92.2% can be attributed to cable only activities in 2002, in comparison to 80.7% in 2001. For the reasons described above, our operating loss from cable activities decreased, from NIS 106.8 million in 2001, to an operating loss of NIS 92.7 million in 2002. Total EBIDTA increased by NIS 57.6 million, from NIS 0.2 million in 2001 to NIS 57.8 million in 2002. The EBITDA from cable activities increased by NIS 39.9 million, or 12.0%, from NIS 19.8 million in 2001, to NIS 59.7 million in 2002. EBITDA from revenue from cable only activities represented 12.0% of our total revenue in 2002 as opposed to 4.2% in 2001.

Net financial expenses. Total net financial expenses decreased by NIS 4.1 million, or 7.7%, from NIS 53.1 million in 2001 to NIS 49 million in 2002. Net financial expenses include interest on our borrowings in Israel and linkage payments related to the fluctuations in the Israeli inflation rate (with respect to our borrowings in shekels, which constitute most of our borrowings) and the US dollar exchange rate (with respect to our borrowings in US dollars). Accordingly, our net financial expenses are affected by the level of our borrowings, from time to time, by changes in the interest rates announced by the Governor of the Bank of Israel and as determined by our creditors, and by changes in the Israeli inflation rate and the exchange rate of the US dollar against the shekel.

Other income. Other income is mainly due to the sale of approximately 50% of our holdings in Partner in April 2002. See Item 4B. Information on the Company Business Overview Cellular Telecommunication Services and Note 16 (d) in our financial statements.

Taxes on income. Costs related to taxes on income increased by NIS 110.5 million, or from NIS 0.4 million in 2001 to NIS 110.0 million in 2002. This increase is primarily due to a capital gain derived form the sale of approximately 50% of our shares in Partner Communications Company Ltd. in April 2002. See Note 14 in our financial statements.

Equity in earnings (losses) of affiliated companies, net. Our share in the losses of affiliated companies decreased by NIS 91.4 million, from a loss of NIS 80.3 million in 2001 to earnings of 11.1million in 2002, mainly due to Partner s gains in 2002, as opposed to its losses in 2001.

Cash Flow

Net cash used in our operating activities in 2002 (for both cable and Internet activity combined), was NIS 91.9 million compared with NIS 19.1million (for both cable and Internet activity combined) provided by our operating activities in 2001.

Net cash provided by our investing activities in 2002 was NIS 233.6 million compared with NIS 239.8 million we used in our investing activities in 2001. Our investing activities are shown in the table below:

	2002	2001
NIS in million		
Purchase of fixed assets	(78.8)	(258.2)
Investment in affiliated companies (shares and capital notes)	0	(3.6)
Repayment of long-term loans to affiliated companies	0.5	0
Deposit of trust, net	1.9	0
Investment in other assets	(3)	(1.1)
Proceeds from sales of investment in affiliated companies	311.7	21
Proceeds from sales of fixed assets	1.3	2.1
Net cash provided by (used in) investing activities	233.6	(239.8)

Net cash used in finance activities in 2002 was NIS 134.4 million compared to NIS 219.5 million provided by finance activities in 2001.

Net increase in cash and cash equivalent was NIS 7.2 million in 2002, compared to a net decrease in cash and cash equivalent of NIS 1.1 million in 2001.

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Year Ended December 31, 2001 compared with Year Ended December 31, 2000

The following table sets forth for the year 2001 our consolidated statement of operation according to our various business segments:

	Adjusted new Israeli shekels in millions		
	Cable TV	Internet	Total
Revenue	472.7	5.6	478.4
Operating expenses	470.4	23.1	493.5
Gross profit (loss)	2.3	(17.5)	(15.1)
Selling and Marketing expenses	56.1	3.0	59.1
General and Administrative expenses	53.0	5.1	58.1
Operating loss	(106.8)	(25.6)	(132.3)

Financial expenses, net	50.1	2.9	53.1
Loss after Financial expenses	(156.9)	(28.5)	(185.4)
Other income, net	1.5	1.6	3.1
Loss before taxes on income	(155.4)	(26.9)	(182.3)
Taxes on income	0.4		0.4
Loss from operation of the Company and its subsidiaries	(155.0)	(26.9)	(181.9)
Equity in losses of affiliated companies, net	80.3		80.3
Net loss	(235.3)	(26.9)	(262.2)
EBITDA	19.8	(19.6)	0.2

As of January 2000, we introduced a new Internet business as an Internet service provider, which was subsequently discontinued in July 2001 and was a significant cause of losses in the year 2000. The termination of this activity in July 2001 eliminates losses that were attributable to this activity. The comparative discussion below presents total activities, and cable only activities as a percentage of such total activities, and (with the exception of cash flow) compares cable only activities in 2001 with cable only activities in 2000.

Revenue. Total Revenue decreased by NIS 5.4 million, or 1.1%, from NIS 483.8 million in 2000 to NIS 478.4 million in 2001. Of the total revenue, approximately 98.8% can be attributed to cable only activities in 2001, in comparison to 99.6% in 2000. Our revenue from cable activities decreased by NIS 9.2 million, or 1.9%, from NIS 481.9 million in 2000 to NIS 472.7 million in 2001. Approximately 95% out of our revenue from cable activities in the year 2001 derived from monthly subscription fee, the rest from depreciation of subscribers deposits for set-top boxes, from installation fees, Pay-Per-View services and payments from the Shopping Channel. The decrease reflects the erosion of the subscription fee due to the effect of inflation, and a reduction in our subscriber base from approximately 301,000 subscribers at December 31 2000, to approximately 292,000 subscribers at December 31, 2001.

Operating expenses. Total operating expenses increased by NIS 75.2 million, or 18.0%, from NIS 418.3 million in 2000 to NIS 493.5 million in 2001. Of the total operating expenses, approximately 95% can be attributed to cable only activities in 2001, in comparison to 93.7% in 2000. As a percentage of revenue from cable only activities, operating expenses from cable only activities increased from 81.3% in 2000 to 99.5% in 2001. Our operating expenses from cable only activities (excluding depreciation and amortization of fixed assets) increased by NIS 52.3 million, or 18.8%, from NIS 279 million in 2000, to NIS 331.3 million in 2001. As a percentage of revenue from cable only activities, operating from cable only activities expenses (excluding depreciation and amortization of fixed assets) increased from 58.0% in 2000 to 70.1% in 2001. The increase in operating expenses from cable only activities (excluding depreciation and amortization of fixed assets) is mainly derived from an increase in programming costs, as set forth below.

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Cable television programming expenses increased by NIS 46.8 million, or 25.8 %, from NIS 181.5 million in 2000, to NIS 228.3 million in 2001. Our cable television programming expenses increased from 37.7% of our total revenue in 2000, to 48.3% in 2001. The increase in programming expenses reflects the launch in the second half of 2001 of tiering services, which produces additional revenue by either purchase of individual channels or packages. As a result of our promotion and marketing activities relating to the tiering services and these channels, the revenue aspect of these services shall only be reflected in our future financial results. In US dollar terms, we do not expect to incur any future increase in programming expenses. However, since all of our programming expenses are either paid in US dollars or linked to US dollars, any substantial devaluation of the shekel against the US dollar will increase the shekel cost of our US dollar denominated expenses.

Depreciation and amortization of fixed assets increased by NIS 26.1 million or 23.1%, from NIS 112.9 million in 2000, to NIS 139 million in 2001. The increase in depreciation and amortization of fixed assets reflects the continuation of investment in large projects requiring intensive capital expenditures undertaken in the years 2000 and 2001. These projects were principally: upgrading cable network bandwidth from 550 MHz to 860 MHz; converting the broadcasting system from analog to digital; and the purchase of new digital set top boxes.

Other operating expenses from cable activities increased by NIS 5.5 million, or 5.7%, from NIS 97.6 million in 2000, to NIS 103.1 million in 2001.The increase in other operating expenses reflects the increase in salaries and maintenance costs related to the deployment of new sophisticated and more complicated systems.

Selling and marketing expenses. Total selling and marketing expenses decreased by NIS 6.9 million, or 10.5% from NIS 66.0 million in 2000, to NIS 59.1 million in 2001. Of the total selling and marketing expenses, approximately 95% can be attributed to cable only activities in 2001, in comparison to 81.9% in 2000. Our selling and marketing expenses for cable activities increased by NIS 2 million, or 3.7%, from NIS 54.1 million in 2000, to NIS 56.1 million in 2001. As a percentage of total revenue from cable only activities, our selling and marketing expenses increased from 11.2% in 2000, to 11.9% in 2001.

General and administrative expenses. Total general and administrative expenses decreased by NIS 4.1million, or 6.6%, from NIS 62.2 million in 2000, to NIS 58.1 million in 2001. Of the total general and administrative expenses, approximately 91.2% can be attributed to cable only activities in 2001, in comparison to 81.5% in 2000. Our general and administrative expenses for cable activities increased by NIS 2.3 million, or 4.6%, from NIS 50.7 million in 2000, to NIS 53 million in 2001. As a percentage of total revenue, our general and administrative expenses from cable activities decreased from 10.5 % in 2000 to 11.2% in 2001.

Operating loss and EBITDA. Total operating loss increased by NIS 69.5 million, or 110.7%, from NIS 62.8 million in 2000, to NIS 132.3 million in 2001. Of the total operating loss, approximately 80.7% can be attributed to cable only activities in 2001, in comparison to 23.5% in 2000. For the reasons described above, our operating loss from cable activities increased, from NIS 14.8 million in 2000, to an operating loss of NIS 106.8 million in 2001. Total EBIDTA decreased by NIS 45.2 million from NIS 45.4 million in 2000 to NIS 0.2 million in 2001. The EBITDA from cable activities decreased by NIS 70.2 million, or 78%, from NIS 90 million in 2000, to NIS 19.8 million in 2001. EBITDA from revenue from cable only activities represented 4.2% of our total revenue in 2001, as opposed to 18.7% in 2000.

Net financial expenses. Total net financial expenses increased by NIS 18.1 million, or 51.7%, from NIS 35.0 million in 2000 to NIS 53.1 million in 2001. The increase in these financial expenses was primarily due to a substantial increase in our outstanding bank credit from NIS 463 million at December 31, 2000 to NIS 687 million at December 31, 2001. Net financial expenses include interest on our borrowings in Israel and linkage payments related to the fluctuations in the Israeli inflation rate (with respect to our borrowings in shekels, which constitute most of our borrowings) and the US dollar exchange rate (with respect to our borrowings in US dollars). Accordingly, our net financial expenses are affected by the level of our borrowings, from time to time, changes in the interest rates announced by the Governor of the Bank of Israel and as determined by our creditors, and by changes in the Israeli inflation rate and the exchange rate of the US dollar against the shekel.

Other income. See Note 16(d) in our financial statements.

Taxes on income. Costs related to taxes on income decreased by NIS 0.6 million, or from NIS 0.2 million costs in 2000 to revenue of NIS 0.4 million in 2001.

Equity in earnings (losses) of affiliated companies, net. Our share in the losses of associated companies decreased by NIS 50.7 million, from NIS 131 million in 2000 to 80.3 million in 2001, mainly due to reduction in Partner s losses.

Cash Flow

Net cash provided by our operating activities in 2001 (for both cable and Internet activity combined), was NIS 19.1million compared with NIS 7.1 million (for both cable and Internet activity combined) that we used in our operating activities in 2000.

The increase in cash flow from operating activities in spite of the increase in losses is due to depreciation and amortization and due to changes in operating asset and liability items in 2001.

Net cash we used in our investing activities in 2001 was NIS 239.8 million compared with NIS 401.3 million we used in our investing activities in 2000. Our investing activities are shown in the table below:

	2001	2000
NIS in million		
Purchase of fixed assets	(258.2)	(375.9)
	(3.6)	(31.4)

Investment in affiliated companies (shares and capital notes)		
Investment in other assets	(1.1)	0
Proceeds from sales of investment in affiliated companies	21	0
Proceeds from sales of investment in other companies	0	5.3
Proceeds from sale of fixed assets	2.1	0.7
Net cash provided by (used in) investing activities	(239.8)	(401.3)

Net cash provided by finance activities in 2001 was NIS 219.5 million compared to NIS 240.1 million provided by finance activities in 2000. The sum used to finance our activities in 2000 includes NIS 226 million as a dividend paid on January 26, 2000. In 2001 we did not distribute a dividend.

Net decrease in cash and cash equivalent was NIS 168.4 million and NIS 1.1 million in the years 2000 and 2001, respectively.

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5B. Liquidity and Capital Resources

We have financed our operations through cash we generated from our operations, equity contributions and loans from our principal shareholders, borrowings from banks and suppliers credit and from the public offerings, in Israel of our ordinary shares on the Tel Aviv Stock Exchange in October 1993 and of debentures and warrants in August 1997, and in the United States of our American Depository Shares in June 1996. Cash flow used in our operations was NIS 91.9 million in 2002 in comparison to cash flow we generated from our operations in 2001 of NIS 19.1.

In April 2002, we sold 13,778,668 shares (approximately 7.7%) of Partner Communications Company Ltd. to a subsidiary of Hutchison Whampoa Ltd., representing approximately 50% of our holdings in Partner, for a price per share of US$4.5295. We currently own indirectly, approximately 7.42% of the outstanding share capital in Partner Communications Company Ltd. The gross consideration we received was $62,410,477. The gain received for the sale of our shares in Partner is subject to income tax. We have paid approximately NIS 70 million as an advance payment on account of this income tax. See Note 14 of our financial statements. Approximately 72% of our shares in Partner are pledged to banks under pledges unlimited in sum to cover Partner s liabilities in respect of its loans from the banks.

We received net capital contributions from our principal shareholders in the amount of approximately NIS 37 million prior to December 31, 1995. In addition, such shareholders have, from time to time, made loans available to us, although as of December 31, 1997 we had no outstanding balances due to such shareholders. We do not anticipate that equity contributions and loans from our principal shareholders will be a source of capital in the foreseeable future.

During the past several years, we made use of external funds to finance our operating activities, capital expenditures associated with building-out our network and investments in associated companies. We have relied on internal cash flows, equity investments and loans from our principal shareholders, together with loans from banks and the proceeds from the issuance of our ordinary shares, American Depository Shares, debentures and warrants, and credit arrangements with suppliers to provide us with the necessary funding for building-out of our cable television network operating and investing activities. Our net capital expenditures, as determined on a cash basis, were NIS 258.2 million for the year ended December 31, 2001, NIS 78.8 million for the year ended December 31, 2002. This decrease in our capital expenditures is due to large projects relating to infrastructure (such as upgrading the network and the digital infrastructure), which required intensive capital expenditures that were completed in 2001. Our investments in affiliated and other companies (on cash basis, net) were approximately NIS 3.6 million for the year ended December 2001. We did not invest in affiliated and other companies in 2002. (See Note 4 in our financial statements.)

On June 18, 2003 and June 19, 2003, we sold in private transactions in Israel an aggregate amount of 149,177 of our ordinary shares held by our subsidiary Cable Systems Media Haifa-Hadera Ltd., in consideration of an aggregate gross amount of approximately $1.05 million (at an average price per ordinary share of approximately $7.02). Subject to market conditions, we may in the future sell up to an additional amount of 1,194,320 of our ordinary shares held by Cable Systems Media Haifa-Hadera Ltd.

As of December 31, 2002 our borrowings consist of long-term loans from Israeli banks and other sources and debentures issued to the public, all of which are linked to the Israeli consumer price index or the US dollar. Our outstanding long-term loans from banks (including current maturities) as of December 31, 2002, were NIS 166.7 million, bearing interest at rates ranging between 6.2% - 7.0% per annum over the Israeli consumer price index, and NIS 6.6 million linked to the US dollar and bearing interest at LIBOR plus 1.5%. Our outstanding long-term loans from other sources (including current maturities) as of December 31, 2002 were NIS 48.2 million linked to the US dollar and bearing interest at LIBOR plus 1.75%. All of our outstanding long term-loans are scheduled to mature by 2008. See Note 10b of our financial statements. As of December 31, 2002, there was a NIS 135.7 million aggregate principal amount of debentures outstanding. The debentures bear interest at a rate of 3.7% over the Israeli consumer price index, all of which are scheduled to mature by 2006. During the period from January 1, 2003 to December 31, 2003, NIS 111.0 million of the long-term loans and debentures will mature. See Notes 10 and 11 of our financial statements.

As of December 31, 2002 our short-terms loans from Israeli banks (excluding current maturities) consist of NIS 447.3 million bearing interest at rates ranging between 10.35% -10.75% per annum.

As of December 31, 2002, our cash and cash equivalents balance totaled NIS 7.7 million compared to NIS 0.5 million in December 31, 2001. We paid a dividend on January 26, 2000 of approximately NIS 226.0 million. We did not pay a dividend in 2001 and 2002. We have not adopted any dividend distribution policy, and we cannot assure you that we would pay additional dividends in the future.

As of December 31, 2002, our investments in Barak I.T.C. (1995) The International Telecommunications Services Corp. Ltd. totaled NIS 16.6 million. In 2002, we wrote-off approximately NIS 9 million of our investment in Barak, among other things, based on a company valuation of Barak. We may be required to make additional capital contributions in proportion to our relative holdings in Barak in the foreseeable future because Barak may not have readily available financing resources, including from its shareholders.

We provided Bank Leumi a guarantee, in an unlimited amount, for all amounts due from I.C.P. Israel Cable Television Programming Company Ltd., or ICP to such bank, at a rate of 24.6% of the total liabilities due. The board of directors of ICP determined that the total credit to be extended by such bank to ICP shall not exceed $35 million, and any excess amount shall be approved in writing by our board of directors. As at December 31, 2002, the outstanding credit extended by such bank to ICP was NIS 20.2 million. In addition, we are guarantor for ICP towards Bank Hapoalim to secure ICP s liabilities due to such bank, in an amount ranging between approximately $4.2-$6.0 million. We received a demand dated January 26, 2003 from Bank Hapoalim to execute the guarantee.

Since March 26, 2002, Bank Leumi, Bank Igud, Bank Mizrachi, Israel Mercantile Discount Bank and Investec Trust Company have floating charges over all the current and future assets of Matav Cable Systems Media Ltd, and specific fixed charges for an unlimited sum over the unpaid share capital and goodwill of Matav Cable Systems Media Ltd. According to the charge documents, any exercise of the charges shall be subject to the restrictions contained in our Licenses, including the right of the Licensee to use its assets to continue to supply services to its subscribers for so long as such License is valid. Furthermore, any terminal equipment situated in the subscribers premises is exempted from the application of the charge. The provisions of the Telecommunications Law prohibit the grant of a charge over our Licenses.

We commenced negotiations regarding an increase of our present credit lines with our banks, in order to have, together with our internal cash flow, sufficient funds to finance the investment in the continued build-out, development acquisition of additional digital set-top boxes and upgrade of our cable television network. In the framework of our negotiation with the banks regarding the extension of our credit lines, we agreed to enhance the security granted to the banks as collateral for our credit lines by granting a floating charge in their favor, subject to the terms of our Licenses. These negotiations were ceased due to the proceedings in connection with the proposed merger of the Israeli cable television operators, however may be recommenced depending on the progress of the merger or should the merger proceedings cease to continue. Should we recommence such negotiations, there is no assurance that that we shall reach an agreement with the banks and receive such increased credit lines.

In the meantime, we utilize interim financing from the banks. In the event that we shall increase our present credit lines, we expect that the amount and cost of the additional bank credit as well as the security we will be obligated to make available to the banks will be influenced by many factors, including; the absence of private and public markets in debt and equity, our financial results, the effect of competition and regulatory uncertainty. Therefore, we cannot assure you that the additional financing, if any, will be on the same terms as our current financing from the banks, or on terms which are favorable to us or which are not significantly expensive.

Impact of Inflation and Exchange Rate Fluctuations

Our financial statements are presented in shekels, adjusted to reflect changes in the Israeli consumer price index. Consequently, all shekel amounts set forth in our historical financial statements are adjusted each time that we publish new financial statements in order to reflect changes in the Israeli consumer price index as of the date of the latest balance sheet presented. See Note 2 to the financial statements. Since we may not be permitted to raise our fees pursuant to our Licenses in a manner that would fully compensate for any increase in the Israeli consumer price index, inflation in Israel may have a material adverse impact upon us.

Substantially all of our revenues and a majority of our operating expenses are denominated in shekels. However, through December 31, 2002, a substantial amount of our operating expenses were linked to non-shekel currencies. These expenses related mainly to programming where the price paid by us is based on the US dollar. A substantial majority of our capital expenditures are incurred in, or linked to, non-shekel currencies, mainly US dollars. Thus, any devaluation of the shekel against the US dollar, will also increase the shekel cost of our non-shekel denominated or linked expenses. Such increase may have an adverse impact upon our operating results, which may be material. Our borrowings are mostly in Israeli shekels with the remainder in US dollars.

Differences Between Israeli GAAP and U.S. GAAP

Israeli GAAP varies in certain respects from U.S. GAAP. The application of U.S. GAAP to our financial statements would have affected the determination of net loss for the year ended December 31, 2002, and the determination of capital deficiency as of December 31, 2002 to the extent summarized in Note 20 to the financial statements.

5C. Research and Development, Patents and Licenses

Not applicable.

5D. Trend Information

1. In order to further increase our technological and operational efficiencies, we intend to reorganize our current four operational areas in the near future, such that we shall operate our cable television services through two operational areas, Netanya and Haifa. In the framework of this operational reorganization, we will be required to terminate the employment of a certain number of employees and to hire new employees for the expanded operational areas of Netanya and Haifa.

2. For more information about other factors that may affect our results of operations, see Item 3D. Key Information Risk Factors.

ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

6A. Directors and Senior Management

Directors

Set forth below is certain information about our officers and directors as of May 31, 2003.

Directors

Name	Age	Position
Shmuel Dankner	72	Chairman of the Board of Directors
Shimon Cheifetz (1)	60	Director
David Dankner	75	Director
Dor Dankner (1)	42	Director
Leah Dankner	77	Director
Alon Dankner	52	Director
Dr. Zvi Dinstein (2)	76	Director
Hananya Gibstein	69	Director
Michael Goldschmidt (1) (2) (3)	65	Director
David Harnik (1) (2) (3)	60	Director
Zvi Mor	54	Director
Avivi Perlman	42	Director
Meir Srebernik (4)	44	Director
Yehuda Gill	75	Director
Yehoshua Gibstein (1)	43	Alternate Director

Officers

Name	Age	Position
Amit Levin	40	Chief Executive Officer
Ori Gur Arieh	46	Counsel and Company Secretary
Shalom Bronstein	54	Chief Financial Officer
Genia Raichel-Gil	50	Vice President, Customer Service
Meidad Katz	40	Vice President, Engineering
Shlomi Ashkenazi	37	Vice President, Sales, Marketing and Operational Areas
Ron Sharon	47	Vice President, Information Systems

(1) Member of the Finance Committee.
(2) Member of the Audit Committee.
(3) Independent Director.
(4) Since March 2002

Shmuel Dankner has been the chairman of our board of directors since 1988. Mr. Dankner is the chairman of the board of directors of Dankner Investments Ltd., and serves as a director of various companies, including Dor Chemicals Ltd., Israel Salt Company Ltd., Israel Salt Company (Eilat) 1976 Ltd., Dankner Holdings Ltd., Dankner Assets Haifa (1996) Ltd., Dankner Communications Ltd., Dankner Transportation Ltd., Carmel Resins Ltd., Carmel Chemicals Ltd., H.K. Trade Ltd., Conlog Control Ltd., Alex Control Systems Ltd., Israel Salt Industries Ltd., Kirkwood Enterprises Inc., Alcar-Electric Productions Ltd., G.D. Chemicals Ltd., Cable Systems Media Haifa-Hadera Ltd., Matav Investments Ltd., Partner Communications Company Ltd., Matav Infrastructure Ltd., Dor Chembat Ltd., Elran (D.D.) Investments Ltd., Elran (D.D.) Holdings Ltd. and Shamdar Holdings Ltd. Mr. Dankner is the brother of Leah Dankner and David Dankner, the father of Dor Dankner, and the uncle of Alon Dankner and Orli Mor, wife of Zvi Mor.

Alon Dankner has been a director of Matav since July 26, 1999. Mr. Alon Dankner serves as a director in various companies, including: Cable Systems Media Haifa - Hadera Ltd., Matav Investments Ltd., Nave Shoshana Ltd., Israeli Salt Company (Eilat) Ltd., Intact Holdings Ltd., Danran Holdings Ltd., Elran (D.D.) Holdings Ltd., Elran (D.D.) Investments Ltd. and G.D.A.D. Atlit Development Ltd. Mr. Alon Dankner is the nephew of Shmuel Dankner, Leah Dankner and David Dankner, and cousin of Dor Dankner and Orli Mor (wife of Zvi Mor).

Dr. David Dankner has been a director of Matav since July 26, 1999. Dr. David Dankner has been serving as the Chief Executive Officer of Carmel Chemicals Ltd. since 1966. Dr. David Dankner also serves as a director of various companies, including: Dankner Constructions and Development Ltd., Dor Chemicals Ltd., Carmel Resins Ltd., Carmel Chemicals Ltd., Israel Salt Industries Ltd., Israel Salt Company (Eilat) 1976 Ltd., Israel Salt Company Ltd., Alcar-Electric Productions Ltd., G.D. Chemicals Ltd., H.K. Trade Ltd., Conlog Control Ltd., Alex Control Systems Ltd., Salit Salts Ltd., Limor Development Ltd., Unigad Ltd., Dankner Assets Haifa (1996) Ltd., Dor Chembat Ltd., Salt Productions Ltd., Chutzot Hayotzer Ltd., Kastra Ltd., D.G.D Haifa Ltd., Matav Investments Ltd. Cable Systems Media Haifa-Hadera Ltd. Dr. David Dankner is the brother of Shmuel Dankner and Leah Dankner, and the uncle of Alon Dankner, Dor Dankner and Orli Mor (wife of Zvi Mor).

Dor Dankner has been a director of Matav since July 26, 1999. Mr. Dor Dankner also serves as a director in various companies, including: Cable Systems Media Haifa - Hadera Ltd., Matav Assets Ltd., Matav Investments Ltd., Dankner Investments Ltd., Dankner Holdings Ltd., Israel Salt Industries Ltd., Partner Communications Company Ltd., Dankner Elran Infrastructure Ltd., Elran (D.D) Infrastructure Ltd., Elran (D.D.) Real Estate Ltd., Elran (D.D.) Management & Holdings Ltd., Elran (D.D.) Investments Ltd. (as chairman of the board of directors), Elran (D.D.) Holdings Ltd., Elran (D.D.) Technologies Ltd., Elran Gmul Power Stations Ltd., Shachaf Dan Investments Ltd., Cap Ventures Ltd., Dankner Communications Ltd. and Carmel Assets Ltd. In addition, Mr. Dor Dankner serves as Chief Executive Officer of D.S.D. Investments Ltd. Mr. Dor Dankner is the son of Shmuel Dankner, and the nephew of Leah Dankner and David Dankner, and the cousin of Alon Dankner and Orli Mor (wife of Zvi Mor).

Dr. Zvi Dinstein has been a director of Matav since August 14, 1987. Since 1985 Dr. Dinstein has been the Chairman of the board of directors of the Belfer Center for Energy Research, which grants research funding and operates in cooperation with the Israeli Ministry of National Infrastructure and the Ministry of Environment. Dr. Dinstein is also the chairman of the board of directors of Dorot Properties and Holdings Ltd., and director of various companies, including The Israel Phoenix Assurance Company Ltd., Hadar Insurance Company Ltd., Cable Systems Media Haifa - Hadera Ltd., Matav Investments Ltd. and F.I.B.I. Holding Company Ltd. Dr. Dinstein is also a member of the Board of Governors of the Tel Aviv University, the Weizmann Institute of Science and The Hebrew University of Jerusalem.

Leah Dankner has been a director of Matav since September 17, 1997. Ms. Leah Dankner also serves as a director of Cable Systems Media Haifa- Hadera Ltd., Matav Investments Ltd., Dankner Investments Ltd., Dor Chemicals Ltd., Carmel Chemicals and the Israel Salt Industries

Ltd., Kikar Leah Hanynon Ltd. and G.D. Chemicals Ltd., Ms. Leah Dankner is the sister of Shmuel Dankner and David Dankner and the aunt of Alon Dankner, Dor Dankner and Orli Mor, wife of Zvi Mor.

Hanania Gibstein has been a director of Matav since August 14, 1987. Mr. Gibstein also serves as a director of Cable Systems Media Haifa - Hadera Ltd. and Matav Investments Ltd. Mr. Gibstein was a member of the Municipal Council of the city of Rishon Le-Zion, and was the mayor of that city from 1969 to 1983. Mr. Gibstein is the chairman of the Society of Friends of The Beer Yaacob Mental Health Center. Since 1991 Mr. Gibstein has been the vice-chairman of the Association for Welfare of the Soldiers of Israel, and has managed private businesses, primarily in real estate.

Shimon Cheifetz has been a director of Matav since January 20, 1989. Mr. Cheifetz is also a director of various companies in Israel: Matav Investments Ltd., Cable Systems Media Haifa-Hadera Ltd., Matav Assets Ltd. and Barak I.T.C.- The International Telecommunications Services Ltd. Mr. Cheifetz served as the general manager of Maariv-Modiin Publishing House Ltd. until April 1992. Since April 1992 Mr. Cheifetz has been the chairman of the board of directors and a director in various other companies including, Mifratz Flour Mills Ltd., Man Haifa Bay Flour Mills (1999) Ltd., Grand Moulins D Israel Ltd., Ugda Investment Ltd., Synet Industries Ltd., El-Mul Technologies Ltd., Fabia Engineering Ltd., Yeda Research and Development Co. Ltd. and I.G.D. Ltd.

David Harnik has been an outside director of Matav since June 7, 1999. Mr. Harnik, a lawyer by profession, serves as the Vice President of The Olympic Committee of Israel and as the Chairman of the Israel Tennis Association. Mr. Harnik serves as a director of the National Sport Center, The Marine Trust Ltd., and as an independent director of Kanafaim Arkia Holdings Ltd. Mr. Harnik served as the Chief Executive Officer of the Government Tourist Corporation between 1993 and 1998 and served as the Director General of the Tel Aviv Foundation, which engages in development of projects, between January 1999 and December 2002. Mr. Harnik s candidacy for the nomination was approved by the statutory committee of outside directors of the Israeli Securities Authority on May 9, 1999.

Michael Goldschmidt has been an outside director of Matav since June 7, 1999. Mr. Goldschmidt is the Chief Executive Officer and the owner of EMRT Holdings & Business Development Ltd., which engages in holdings and developments of businesses. Mr. Goldschmidt serves as a director of Trans Security Systems & Technology Ltd. Mr. Goldschmidt served as the Chief Executive Officer of The Electric Wire & Cable Company of Israel Ltd. between March 1990 and 1998. Mr. Goldschmidt s candidacy for the nomination was approved by the statutory committee of outside directors of the Israeli Securities Authority on April 18, 1999.

Zvi Mor has been a director of Matav since September 17, 1997. Mr. Mor serves as the Chairman of Dor Gaz Ltd. Mr. Zvi Mor also serves as a director in various companies, including: Dankner Investments Ltd., the Israel Salt Industries Ltd., Carmel Chemicals Ltd., Dor Chemicals Ltd., Dankner Assets Haifa (1996) Ltd., Cable Systems Media Haifa - Hadera Ltd. and Matav Investments Ltd. Mr. Zvi Mor is married to Orly Mor (Gineo), niece of Shmuel Dankner, Leah Dankner and David Dankner, and cousin of Alon Dankner and Dor Dankner.

Avivi Perlman has been a director of Matav since October 2001. Mr. Perlman also serves as a director of Matav Investments Ltd. and Cable Systems Media Haifa Hadera Ltd. Mr. Perlman served as the legal counsel of Dankner Investments Ltd. between February 2001 and April 15, 2003.

Meir Srebernik has been a director of Matav since March 2002. Mr. Srebernik is the Chief Executive Officer of Dankner Investments Ltd., since February 2002. Mr. Srebernik serves as a director of various other companies, including Dankner Assets Ltd., Dankner Assets Haifa (1996) Ltd., Dankner Constructions and Development Ltd., Dankner Investments in Real Estate (USA) Ltd., Neot Dankner Maintenance & Services (1982) Ltd., Drorim Mall Ltd., Rehovot Shopping and Transport Center Management Company Ltd., Dankner Transportation Ltd., Dankner Communications Ltd., Dankner Holdings Ltd., Shalom Industrial Park Ltd. and Nonstop Ventures Ltd. Between 1995 and 2000, he was the president and Chief Executive Officer of Netia Holding SA, a leading Polish alternative fixed line telecommunications company. He has also served as the head of the cable television division of the Israeli Ministry of Communications, as Vice President of Telecommunications of Dankner Investments Ltd. and as a director of Pelephone Communications Ltd., one of the four mobile phone service providers in Israel.

Yehuda Gill has been a director of Matav since November 2001. Mr. Yehuda Gill also serves as a director of Union Bank of Israel Ltd. Since 2001, Mr. Gill serves as the managing director and executive vice chairman of Israel Oil Prospectors Corporation Ltd.

Yehoshua Gibstein has been an alternate director of Matav for Mr. Hanania Gibstein since May 24, 1998. Mr. Yehoshua Gibstein was a director of Matav between 1992 and May 1998. Mr. Gibstein is also a director in Pikom Ltd., Exent Technologies Ltd., Cabletek Ltd. and Noa (G.P.A) Investment Company Ltd., which specializes in investment and project development. Mr. Gibstein is the son of Hanania Gibstein.

Amit Levin has been our Chief Executive Officer since October 7, 1999. Before that and since September 1998, he served as our interim Chief Executive Officer. Between October 1994 and September 1998, he was Matav s Vice President of Israeli Operations. Mr. Levin is a director of

Nonstop Internet (1999) Ltd., Matav Assets Ltd. and Matav Infrastructure Ltd. Between 1991 and 1994, Mr. Levin was Matav s area manager for Netanya.

Ori Gur Arieh has been Matav s Counsel and Company Secretary since November 2000. Prior to his employment with Matav, Mr. Gur Arieh was a partner in the private law practice of Avital, Dromi & Co.

Shalom Bronstein has been our Chief Financial Officer since 1989. Prior to 1989, Mr. Bronstein was vice president of finance of SI Holdings Ltd., an industrial, construction and real estate company.

Genia Raichel-Gil has been Matav s Vice President of customer service since February 2000. Before that and since November 1994, she served as an operating area manager of our Netanya and Haifa franchise areas.

Meidad Katz has been Matav s Vice President of engineering since 1996. Before that he served as a hardware engineer at ECI Telecom Ltd. in their SDH (Synchronous Digital Hierarchy) Telecom department.

Shlomi Ashkenazi has been Matav s Vice President of sales, marketing and operational areas since August 2002. Between February 2002 and August 2002 he served as Matav s Vice President of sales and operational areas. Before that and since 1998, he served as Matav s Vice President and Chief Operating Officer. Between 1995 and 1998 he served as an operating area manager for our Bat-Yam, Holon and the Galilee franchise areas.

Ron Sharon has been Matav s Vice President of information systems since November 2000. Before that and since May 1998, he worked at Hamashbir Fashion House Ltd. as their information system officer.

Under the shareholders agreement dated October 18, 1993, as amended in July 2002, to which Dankner Investments Ltd., Mr. Hanania Gibstein, Mr. Eli Cheifetz, Mr. Shimon Cheitetz and Dr. Zvi Dinstein, and the companies controlled by such parties that hold our ordinary shares are currently parties, certain of our shareholders have agreed to vote their respective shares in a manner that would enable each of such shareholders to appoint a number of directors to our board of directors in proportion to each of such shareholder s holdings in our company as compared with the original holdings of all parties to this agreement. All of our current directors, except our current outside directors, have been designated to serve as members of our board of directors pursuant to this shareholders agreement. For additional information regarding the shareholders agreement, see Item 7A. Major Shareholders and Related Party Transactions Major Shareholders - Matav Shareholders Agreements .

Except as disclosed above, none of the above directors or members of senior management has any family relationship with any other director or senior manager of Matav.

6B. Compensation

The aggregate net compensation paid, and benefits in kind granted to or accrued on behalf of all of our directors, officers and members of our extended management, as a group, for their services in all capacities during the year ended December 31, 2002 (23 persons of which 4 are directors) was approximately NIS 11.0 million. This amount includes $50,000 that was paid to Mr. Dor Dankner, a member of our board of directors, for his services over the years since 1998 on our behalf in connection with Partner Communications Company Ltd. (including, among other things, with regard to the sale of approximately half of our holdings in Partner Communications Company Ltd. during April 2002). This amount excludes amounts we expended for automobiles we made available to our officers and members of extended management and expenses (including business travel, professional and business association dues and expenses) with which we reimbursed our officers and members of extended management.

In addition, as of December 31, 2002, options were granted to our senior management under our 1997 Senior Employee Share Option Plan, or the 1997 Plan, to purchase up to 71,100 of our ordinary shares, at an exercise price of $8 per share. In January 2003, the 1997 Plan terminated and all of the outstanding options granted under the 1997 Plan expired. Additionally, for the period ending May 31, 2003, options were granted to our senior management under our 2001 Senior Employee Option Plan, or the 2001 Plan, to purchase up to an aggregate 696,334 of our ordinary shares or 348,167 ADSs, which vest in three equal portions, at an exercise price, with respect to the first vested portion, of NIS 40 per ordinary share or NIS 80 per ADS, and with respect to the second and third vested portions, of NIS 49 per ordinary share or NIS 98 per ADS. Each portion of the options granted under the 2001 Plan are exercisable within 24 months after such portion first becomes exercisable, subject to earlier expiration upon the termination of employment under certain circumstances. For more information, see Item 6E. Directors, Senior Management and Employees Share Ownership .

We do not compensate our directors who are not officers, except for Michael Goldschmidt, David Harnik and Yehuda Gill, for their services as members of our board of directors and its committees. We continue to record expenses in our financial statements in relation to the bonus incentive agreements we entered into with each of Mr. Uri Levit and Mr. Moshe Gavish in connection with their prior service as vice chairman of our board of directors.

6C. Board Practices

Israeli Companies Law

We are subject to the provisions of the Israeli Companies Law, 5759-1999, which became effective on February 1, 2000 and regulations adopted thereunder, which supersede most of the provisions of the Israeli Companies Ordinance (New Version) 5743-1983.

Terms of Directors

Generally, directors are elected at the annual or other general shareholders meeting to serve for 3 years, in the case of outside directors, or until the next annual or general shareholders meeting, in the case of other directors, or until their respective successors are elected and qualified, whichever occurs first. Since our current outside directors were appointed pursuant to the provisions of the Companies Ordinance [New Version], 5443 - 1983, their term ends on June 6, 2004, after which time new outside directors will be appointed for a term of 3 years. Currently, our articles of association provide that our board of directors consists of at least 4 directors but not more than 15. Our articles of association provide that a majority of our board of directors, entitled to participate, may appoint additional directors, up to the maximum number permitted. Our articles of association also provide that our board of directors may delegate all of its powers to committees of the board of directors, as it deems appropriate, subject to the provisions of the Companies Law. No director has a service contract with our company or its subsidiary providing for benefits upon termination of employment. Our officers serve at the discretion of our board of directors or until their successors are appointed.

Alternate Directors

Our articles of association provide that a director may at any time, appoint any individual as an alternate director. In addition, no person who already serves as a director or alternate director of Matav may serve as the alternate director of another director of Matav. An alternate director may not serve as such unless such person is qualified to serve as a director. Under the Companies Law, an alternate director shall have all of the rights and obligations of the director appointing him or her. The alternate director may not act at any meeting at which the director appointing him or her is present. Unless the time period or scope of any such appointment is limited by the appointing director, such appointment is effective for all purposes and for an indefinite time, but will expire upon the expiration of the appointing director s term. Mr. Yehoshua Gibstein is alternate director for Mr. Hanania Gibstein, in his absence.

Independent Directors and Outside Directors

Pursuant to the listing requirements of the Nasdaq National Market, we are required to have at least 2 independent directors on our board of directors and to establish an audit committee.

The Companies Law requires that we have 2 outside directors. The election of an outside director under the Companies Law must be approved by a general meeting of shareholders provided that either: (a) the majority of shares voted at the meeting, including at least one third of the shares of non-controlling shareholders voted at the meeting, vote in favor of such election; or (b) the total number of shares voted against such election does not exceed one percent of the aggregate voting rights in the company.

Mr. David Harnik and Mr. Michael Goldschmidt are our current outside directors who satisfy the provisions of the Companies Ordinance pursuant to which they were appointed, and also satisfy the requirements of the Nasdaq National Market regarding independent directors. After the end of their term on June 6, 2004, new outside directors will be appointed in accordance with the provisions of the Companies Law.

Audit Committee

The Companies Law requires public companies, including us, to appoint an audit committee. The responsibilities of the audit committee include reviewing our financial statements, identifying irregularities in the management of the company s business (including in consultation with the internal auditor and the company s independent accountants) and to suggest an appropriate course of action to amend such irregularities, and approving certain related party transactions as required by law. An audit committee must consist of at least 3 members, and include all of the company s outside directors. However, the chairman of the board, any director employed by the company or providing services to the company on an ongoing basis, any controlling shareholder or any relative of a controlling shareholder, may not be a member of the audit committee. The current members of our audit committee are: Mr. Zvi Dinstein, Mr. Michael Goldschmidt and Mr. David Harnik.

Internal Auditor

The Companies Law requires the board of directors of a public company to appoint an internal auditor proposed by the audit committee. A person who does not satisfy certain independence requirements may not be appointed as an internal auditor. The role of the internal auditor is to examine, among other things, the compliance of the company s conduct with applicable law and orderly business procedures. Mr. Eli Blatt was appointed as our internal auditor in January 2000. Mr. Blatt is also the internal auditor of Dankner Investments Ltd., one of our major shareholders.

Fiduciary Duties of an Office Holder

The Companies Law imposes fiduciary duties on an office holder of a company, which consist of a duty of loyalty and a duty of care. An office holder is defined in the Companies Law as a director, general manager, chief executive officer, executive vice president, vice president, other manager directly subordinate to the any other person assuming the responsibilities of any of the foregoing positions regardless of that person s title and other managers directly subordinate to the general manager. The duty of loyalty requires the office holder to avoid any conflict of interest between the office holder s duties for the company and other duty or personal affairs, and proscribes any competition with the company or the exploitation of any business opportunity of the company in order to receive personal advantages for himself or herself, or for others. This duty also requires him or her to reveal to the company any information or documents relating to the company s affairs that the office holder has received due to his or her position as an office holder. The duty of care requires an office holder to act with the level of care which a reasonable office holder in the same position would employ under the same circumstances. This includes the duty to utilize reasonable means to obtain information regarding the advisability of a given action submitted for his or her approval or performed by virtue of his or her position, and all other relevant information pertaining to such action.

Approval of Related Party Transactions

Generally, under the Companies Law the compensation of office holders who are directors requires the approval of the audit committee, the board of directors and the general meeting of the shareholders of the company (in that order). The Companies Law also requires that arrangements as to the compensation of office holders who hold a controlling interest in the company must be approved by the audit committee, the board of directors and a meeting of the shareholders (in that order) provided that either: (a) the majority of shares voted at the meeting, including at least one third of the shares of shareholders not having a personal interest in the matter voted at the meeting, vote in favor of such arrangement; or (b) the total number of shares voted against such arrangement does not exceed one percent of the aggregate voting rights in the company.

The Companies Law requires that an office holder promptly disclose any direct or indirect personal interest that he or his affiliates may have, and all related material information known to him, in connection with any existing or proposed transaction by the company. The office holder must make his disclosure orally or in writing no later than the first meeting of the company s board of directors meeting which discusses the particular transaction. The company may approve the transaction in accordance with the provisions of its articles of association and the Companies Law. Under the Companies Law, if the office holder has a personal interest, the company may approve the transaction provided that the transaction is not adverse to the company s interest. In addition, if the transaction is an extraordinary transaction, then in addition to any approval required by the articles of association, it also must be approved by the company s audit committee, its board of directors (in that order) and, in certain circumstances, the shareholders of the company at a general meeting. Generally, a director who has a personal interest in a matter that is considered at a meeting of the board of directors or the audit committee may not attend that meeting or vote on the matter, unless a majority of the board of directors or the audit committee also has a personal interest in the matter.

For information concerning the direct and indirect personal interests of certain of our office holders and principal shareholders in certain transactions, see Item 7. Major Shareholders and Related Party Transactions.

Under the Companies Law, the disclosure requirements which apply to an office holder also apply to a controlling shareholder of a public company. Moreover, under the Companies Law, extraordinary transactions between a public company and a controlling shareholder of the company or with a third party in which a controlling shareholder has a personal interest, in addition to any approvals stipulated by the articles of association, require the approval of the audit committee, the board of directors and of the shareholders with the same majority requirement as required for the approval of compensation arrangements of office holders who hold a controlling interest in the company.

Duty of a Shareholder

Under the Companies Law, a shareholder has a duty to act in good faith towards the company and other shareholders, and refrain from improperly exploiting his power in the company, including when voting in the general meeting of shareholders on (a) any amendment to the articles of association, (b) an increase of the company s authorized share capital, (c) a merger or (d) approval of transactions with interested parties which require shareholder approval. In addition, any controlling shareholder, any shareholder who knows that it possesses the power to determine the outcome of a shareholder vote and any shareholder that, pursuant to the provisions of the articles of association, has the power to appoint or prevent the appointment of an office holder in the company or any other power towards the company, is under a duty to act in fairness towards the company. The Companies Law does not detail the substance of this duty.

Exculpation of Office Holders

Under the Companies Law, an Israeli company may not exempt an office holder from liability with respect to a breach of his duty of loyalty, but may exempt in advance an office holder from his liability to the company, in whole or in part, with respect to a breach of his duty of care, provided that the articles of association of the company permit it to do so. Our articles of association allow us to exempt our office holders to the fullest extent permitted by law.

Indemnification of Office Holders

Our articles of association permit us to undertake in advance to indemnify our officers and directors, provided that the undertaking is restricted to the events of a kind which the board of directors may anticipate at the time it makes such undertaking and limited to an amount which the board of directors determines is reasonable under the circumstances. In addition, we can indemnify an officer or director for specific occurrences retroactively.

Our articles of association further provide that the total amount as to which we may indemnify our officers and directors under these provisions shall not exceed 25% of our equity according to the last financial statements that were published.

Our articles of association also provide that we may indemnify an officer or director for liability or expense imposed on him as a result of an action performed by him in his capacity as our officer or director as follows:

(1) Any financial liability imposed on the officer or director in favor of a third party in accordance with a judgment, including a judgment given in a settlement or a judgment of an arbitrator, approved by the court.

(2) Reasonable litigation expenses, including legal fees, incurred by the officer or director or which he was ordered to pay by the court:

(a) within the framework of proceedings filed against him by Matav or on Matav s behalf or by a third party,

(b) in a criminal proceeding in which he was acquitted,

(c) in a criminal proceeding in which he was convicted of a felony which does not require a finding of criminal intent.

Insurance of Office Holders

Our articles of association provide that, subject to the provisions of the Companies Law, we may enter into a contract for the insurance of the liability of any of our office holders with respect to an act performed by such individual in his or her capacity as an office holder, for:

(1) a breach of an office holder s duty of care to us or to another person;

(2)

a breach of an office holder s duty of loyalty to us, provided that the office holder acted in good faith and had reasonable cause to assume that his or her act would not prejudice our interests; or

(3) a financial liability imposed upon an office holder in favor of another person.

We have obtained a directors and officers insurance policy, currently valid until July 2003.

Limitations on Exculpation, Indemnification and Insurance

Under the Companies Law, in no event may we enter into a contract for the insurance of our office holders, indemnify an office holder or exempt an officer from responsibility toward the company, for:

(1) breach of the duty of loyalty toward Matav, unless, with respect to insurance coverage, the officer or director acted in good faith and had reasonable grounds to assume that the action would not harm us;

(2) breach of the duty of care if it was committed intentionally or recklessly;

(3) an act or omission committed with the intent to yield a personal profit; or

(4) any fine or penalty imposed on the office holder.

6D. Employees

At December 31, 2002, we had 743 employees on a full-time or full-time equivalent basis (820 at December 31, 2001). Of these employees, 153 were in engineering and technical support (188 at December 31, 2001), 228 were in customer service and support (240 at December 31, 2001), 194 were in marketing (209 at December 31, 2001), 32 were in Internet activities (35 at December 31, 2001), and the remainder in administration, programming and management.

At December 31, 2001, we had 820 employees on a full-time or full-time equivalent basis (855at December 31, 2000). Of these employees, 188 were in engineering and technical support (187 at December 31, 2000), 240 were in customer service and support (231 at December 31, 2000), 209 were in marketing (142 at December 31, 2000), 35 were in Internet activities (161at December 31, 2000), and the remainder in administration, programming and management. The reduction in employees of our Internet activities from 2001 to 2000 was due to reduction of Internet activities in 2001.

As at December 31, 2002, all of our employees are located in Israel.

Substantially all of our employees have entered into employment contracts with us, terminable at will by either party.

Our employees are not covered by any specific collective bargaining agreement. However, we are subject to various Israeli labor laws and practices, as well as orders extending certain provisions of collective bargaining agreements between the Histadrut, currently the largest labor organization in Israel, and the Coordination Bureau of Economic Organizations, the federation of employers organizations. Such laws, agreements and orders cover a wide range of areas and impose minimum employment standards including, working hours, minimum wages, vacation and severance pay, and special issues, such as equal opportunity in employment, and employment of women, youth, disabled persons and army veterans.

We generally contribute funds on behalf of our employees to a fund known as Managers Insurance. This fund provides a combination of savings plan, insurance and severance pay benefits to the employees, giving the employees a lump sum payment upon retirement or a pension upon retirement and securing some of the severance pay, if legally entitled, upon termination of employment. Most of our employees are entitled to participate in the plan upon the start of employment or after an initial period. Each employee contributes an amount equal to 5% of his salary and we contribute between 13.3% and 15% of such employee s salary.

We also offer some of our employees the opportunity to participate in a Continuing Education Fund, which functions also as a savings plan. Each of the participating employees contributes an amount equal to 2.5% of his salary and we contribute 7.5% of such employee s salary.

According to the National Insurance Law, Israeli employers and employees are required to pay predetermined sums to the National Insurance Institute. These contributions entitle the employees to health insurance and benefits in periods of unemployment, work injury, maternity leave, disability, reserve military service and bankruptcy or winding-up of the employer. We have never experienced a strike or work stoppage.

Except for one action pending against us, by a former service provider, claiming an employer-employee relationship existed at the time he provided his services, no material labor-related claims are pending. For more information on this claim, also see Item 8A. Financial Information Consolidated Statements and Other Financial Information Legal and Arbitration Proceedings.

6E. Share Ownership

As of May 31, 2003, our directors owned an aggregate of 3,822,267 or 12.65% of our outstanding ordinary shares. Except for Shimon Cheifetz, Dr. Zvi Dinstein and Hananya Gibstein, no individual director or senior manager listed in Item 6B - Directors and Senior Management, owns directly (or through fully owned companies) 1% or more of our outstanding ordinary shares.

As of December 31, 2002, our senior managers, in the aggregate held options under our 1997 Employee Share Option Plan, or the 1997 Plan, to purchase up to 71,000 of our ordinary shares, at an exercise price of $8 per share. In January 2003, the 1997 Plan terminated and all of the outstanding options granted under the 1997 Plan expired.

As of May 31, 2003, our senior managers, in the aggregate held options under our 2001 Senior Employee Share Option Plan, or the 2001 Plan, to purchase up to 696,334 of our ordinary shares or 348,167 ADSs, which vest in three equal portions, at an exercise price, with respect to the first vested portion, of NIS 40 per ordinary share or NIS 80 per ADS, and with respect to the second and third vested portions, of NIS 49 per ordinary share or NIS 98 per ADS.

As of May 31, 2003, Mr. Hanania Gibstein owned 262,939 ordinary shares or 0.88% of our outstanding ordinary shares directly, and an additional 1,430,356 ordinary shares or 4.73% of our outstanding ordinary shares indirectly, through his holdings in Gibstein Holdings Ltd., Gibstein Financial Holdings (1998) Ltd. and Gibstein Investments (1997) Ltd.

As of May 31, 2003, Messrs. Shimon Cheifetz and Eli Cheifetz owned 625,524 ordinary shares or 2.07% of our outstanding ordinary shares directly, and 710,392 ordinary shares or 2.35% of our outstanding ordinary shares, indirectly through their holdings in Cheifetz Holdings Ltd.

As of May 31, 2003, Dr. Zvi Dinstein owned 596,170 ordinary shares or 1.97% of our outstanding ordinary shares, indirectly through his holdings in Dorot Communications Ltd.

Members of the Dankner and Gineo families are parties to a shareholders agreement in Dankner Investments Ltd., concerning the voting of a part of their respective shares in coordination with the other parties to the agreement. This shareholders agreement will terminate upon the completion of the transactions in connection with the current process of structural reorganization of the Dankner Group. For additional information, see Item 4C. Organizational Structure . Each member of the Dankner and Gineo families who is a party to this agreement could be deemed to be the beneficial owner of all the shares of our ordinary shares owned by Dankner Investments Ltd., but they disclaim beneficial ownership of such shares.

1997 Senior Employee Share Option Plan

In November 1997, our board of directors adopted the 1997 Employee Share Option Plan, or the 1997 Plan, to promote the interests of our company and its shareholders by providing our senior management and other employees with appropriate incentives and rewards to encourage them to enter into and continue in the employ of Matav and to acquire a proprietary interest in our long-term success. In January 2003, the 1997 Plan terminated and all of the outstanding options granted under the 1997 Plan expired.

The 1997 Plan authorized the issuance of options to purchase up to 500,000 of our ordinary shares. As of December 31, 2002 and prior to the termination of the 1997 Plan, we had granted, to 16 of our senior and other employees, options to purchase an aggregate 71,000 of our ordinary shares, at an exercise price of $8 per share, all of which expired upon termination of the Plan in January 2003. Prior to the termination of the 1997 Plan and the expiration of the options granted under the 1997 Plan, 275,000 options were net exercised by our senior employees into 185,153 ordinary shares, representing approximately 37.40% of the number of ordinary shares reserved under the 1997 Plan.

2001 Senior Employee Share Option Plan

On January 30, 2001, our board of directors adopted the 2001 Employee Share Option Plan, or the 2001 Plan, to promote the interests of our company and its shareholders by providing our senior management and other key employees with appropriate incentives and rewards to encourage them to enter into and continue in the employ of Matav and to acquire a proprietary interest in our long-term success. We will not grant options to our directors under the 2001 Plan.

The 2001 Plan currently authorizes the issuance of options to purchase up to 864,000 of our ordinary shares, or 432,000 ADSs. Each option represents the right to receive, upon exercise, our ordinary shares or ADSs in the value of the appreciation, if any, of the price of our ordinary shares on the Tel Aviv Stock Exchange, on the day of exercise, over the exercise price for each ordinary share subject to the option. As of May 31, 2003, we had granted to 40 of our senior and other employees, options to purchase an aggregate of 696,334 of our ordinary shares or 348,167 ADSs, which vest in three equal portions, at an exercise price, (1) with respect to the first vested portion, of approximately NIS 40 per ordinary share and NIS 80 per ADS. These exercise prices represent 90% of the price of our ordinary shares on the Tel Aviv Stock Exchange on August 15, 2001; and (2) with respect to the second and third vested portions, of approximately NIS 49 per ordinary share and NIS 98 per ADS. These exercise prices represent 85% of the price of our ordinary shares on the Tel Aviv Stock Exchange on January 30, 2001 and are linked to the Israeli consumer price index of December 2000 (published January 15, 2001). The exercise price will not be paid to our company, rather will only serve to determine the benefit accruing to these employees from the issuance of the options, and the number of ordinary shares or ADSs exercisable by such employees under their individual options.

The employees right to exercise their options is conditioned upon their having continuously been employed by us from the date of grant of the option and until the option or any portion thereof has vested. Generally, the vesting schedule of the options we grant is as follows: one-third of the ordinary shares underlying the option are exercisable 15 months from the date of the grant, another third is exercisable on the second anniversary of the date of grant, and the remaining third is exercisable on the third anniversary of the date of grant. Each portion of the option may be exercised within two years after such option first become exercisable. As of May 31, 2003, none of the options to purchase ordinary shares or ADS s granted under the 2001 Plan were exercised by our senior employees.

In accordance with Section 102 of the Israeli Income Tax Ordinance (New Version), 1961 and regulations promulgated thereunder, the options and the shares to be issued upon exercise of the options will be held for the benefit of the option holders by a trustee who will hold the outstanding options and any shares issued upon exercise of the options in trust on behalf of each participant for a period of not less than two years from the date the option is issued to the Trustee on behalf of such employee.

An option shall be exercised upon the instruction of an option holder to the Trustee. If an option holder s employment with Matav is terminated in circumstances sufficient to deny the participant severance payment under Israeli Severance Payment Law, 1963, his options will expire upon termination of employment. If an option holder s employment with Matav is terminated for any other reason, he may exercise his vested options within 24 months following their vesting. If an option holder s employment with Matav is terminated as a result of the retirement, death or disability of the option holder, he or his heirs, as the case may be, may exercise his vested options within 24 months following their vesting. If, however, following the termination of employment, Matav learns of a breach by the option holder of his employment agreement, Matav may terminate those options that have vested but not yet exercised.

Our board of directors may, at any time and from time to time, terminate or amend the plan in any respect, subject to any applicable approvals or consents that may be otherwise required by law, regulation or agreement, and provided that no termination or amendment of the plans shall adversely affect the terms of any option which has already been granted.

The ordinary shares issuable upon exercise of the options covered by the 2001 Plan, are registered for sale on both Nasdaq and the Tel Aviv Stock Exchange.

Warrants and Debentures

In August 1997, the Company issued NIS 200 million par value registered debentures, of Series A, for redemption in seven equal installments on every August 20, commencing August 2000. As of December 31, 2002, the net outstanding balance of debentures appearing in our financial statements is approximately NIS 169.3 million.

On August 28, 1997, in connection with the issuance of debentures to the public, we issued warrants, of series one, to the purchasers of our debentures, to purchase an aggregate of 2,850,000 of our ordinary shares. By August 20, 2001 (the expiry date of the warrants), warrants to purchase 2,786,764 ordinary shares had been exercised, for consideration of approximately NIS 137.3 million (out of which we, through a fully owned subsidiary, exercised warrants to purchase 1,370,148 ordinary shares for a total payment of approximately NIS 67.1 million), and warrants to purchase 63,236 ordinary shares had expired.

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Item 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

7A. Major Shareholders

The following table sets forth certain information with respect to the beneficial ownership of our ordinary shares as of June 20, 2003 with respect to each person or entity that we believe to be the beneficial owner of 5% or more of our outstanding ordinary shares. Except where otherwise indicated, we believe, based on information furnished to us by the principal shareholders, that the beneficial owners of the ordinary shares listed below have sole investment and voting power with respect to such ordinary shares.

Name	Number of Ordinary Shares Beneficial Owned	Percentage of Outstanding Ordinary Shares Beneficially Owned	Percentage of Voting Securities (*)
Dankner Investments Ltd. (1)	14,418,918	47.74%	49.70%
Ma ariv Modein Publishing House Ltd. (2)	4,556,803	15.09%	15.70%
Hanania Gibstein	1,693,295	5.61%	5.84%

*taking into consideration the 1,194,320 of our ordinary shares held by Cable Systems Media Haifa - Hadera Ltd (our fully owned subsidiary) as at June 20, 2003 which do not have voting rights for so long as such shares are held by Cable Systems Media Haifa-Hadera Ltd. (in accordance with the Israeli Companies Law, which states that if a subsidiary buys shares in the parent company, such shares will not carry voting rights, so long as they are owned by the subsidiary).

(1) Dankner Investments Ltd. owns 47.74 % of our ordinary shares directly. Dankner Investments Ltd. is a publicly held company, whose securities are traded on the Tel Aviv Stock Exchange, controlled by members of the Dankner and Gineo families (who collectively hold approximately 88.19% of Dankner Investments Ltd. issued share capital). Members of the Dankner and Gineo families are parties to the shareholders agreement in Dankner Investments Ltd., concerning the voting of part of their respective shares in coordination with the other parties to the agreement. This shareholders agreement will terminate upon the completion of the transactions in connection with the current process of structural reorganization of the Dankner Group. For additional information, see Item 4C. Organizational Structure . Each member of the Dankner and Gineo families who is a party to the Dankner shareholders agreement could be deemed to be beneficial owners of all of our ordinary shares owned by Dankner Investments Ltd., but except to the extent of their pecuniary interest in such shares, they disclaim beneficial ownership of such shares. This shareholders agreement will terminate upon the completion of the transactions in connection with the current process of structural reorganization of the Dankner Group. For additional information, see Item 4C. Organizational Structure . Shmuel Dankner, the chairman of our board of directors, owns 3.46% of the share capital of Dankner Investments Ltd. and together with Roz Dankner, owns an additional 0.79% of such share capital and together with Dor Dankner, owns an additional 0.04% of such share capital. David Dankner, one of our directors, owns 3.09% of the share capital of Dankner Investments Ltd. and together with Erlen Roda Dankner, owns an additional 1.4% of such share capital. Alon Dankner, one of our directors, owns 1.07% of the share capital of Dankner Investments Ltd. Leah Dankner, one of our directors, owns 18.18% of the share capital of Dankner Investments Ltd. Zvi Mor, one of our directors, is married to Orly Mor, who owns 5.35% of the share capital of Dankner Investments Ltd. Dor Dankner, one of our directors, owns approximately 1.94% of the share capital of Dankner Investments Ltd. and together with Shmuel Dankner, owns an additional 0.04% of such share capital. In addition, Shmuel Dankner, Abraham Dankner, David Dankner, Leah Dankner, Rachel Elran and Orly Mor (wife of Zvi Mor), collectively own, together, 29.71% of the share capital of Dankner Investments Ltd. Each of Shmuel Dankner, Abraham Dankner, Rachel Elran, Leah Dankner, Dor Dankner and Zvi Mor are directors on the board of directors of Dankner Investments Ltd.

(2) Ma ariv Modein Publishing House Ltd. is a company fully owned by Ma ariv Holdings Ltd. Dankner Investments Ltd. own approximately 3.43% of Ma ariv Holdings Ltd. 61.73% of the issued share capital of Ma ariv Holdings Ltd. is directly and indirectly owned by The Israel Land Development Company Ltd., or the ILDC , a public company whose securities are traded on the Tel Aviv Stock Exchange. The ILDC is directly and indirectly controlled by Mr. Jackob Nimrodi (68.08% in voting power and 36.16% in share capital). Accordingly, Mr. Nimrodi could be deemed to be beneficial owner of our ordinary shares owned by Ma ariv Modein Publishing House Ltd., but Mr. Nimrodi disclaims beneficial ownership of such shares. 27.19% of the issued share capital of Ma ariv Holdings Ltd. is held by Mr. Vladimir Gusinsky. Our Cable Broadcast Licenses include a comment stating that the Council has considered including a provision in these Licenses, whereby Ma ariv Holdings Ltd. or its current controlling shareholder will cease to be the beneficial owner of 5% or more of our outstanding ordinary shares, due to the certain convictions of Mr. Jackob Nimrodi for criminal offenses according to the Telecommunications Law; however, due to the fact that the merger of

the Israeli television operators has been approved by the Council and the Commissioner of Restrictive Business Practices, and to the Council s best knowledge, these operators intend to effect the merger, and since such a merger would nullify the necessity for such a provision, the Council decided to grant these Licenses without, at such stage, including such a provision; in the event that the merger will not be consummated by February 28, 2003, or in the event that following the merger Ma ariv Holdings Ltd. will be an interested party of the merged entity, the Council will reconsider the integration of such a provision into our Licenses. The Council recently approached us in this regard, following which there have been exchanges of correspondence between the Council and us. We have expressed our objection to including such a provision in our Licenses, due to, among other things, the fact that we do not have the right or any other legal means to force a shareholder to sell its shares in Matav.

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(3) Mr. Hanania Gibstein holds directly approximately 0.87% percent of our ordinary shares and approximately 4.74% of our ordinary shares are held by companies fully owned by Mr. Gibstein (of which approximately 1.3% is held by Gibstein Investments (1997) Ltd., approximately 3.42 % is held by Gibstein Holdings Ltd. and approximately 0.01% is held by Gibstein Financial Holdings (1998) Ltd.). Mr. Hanania Gibstein serves as a director on our board of directors.

Matav Shareholders Agreements

1. Prior to our initial public offering on Nasdaq on October 19, 1993 and on the Tel Aviv Stock Exchange, on October 18, 1993, Dankner Investments Ltd., Mr. Hanania Gibstein, Hapoalim Electronic Communications Ltd., Ma ariv Electronic Communications, Shamrock Holdings of California Inc., Mr. Eli Cheifetz, Mr. Shimon Cheifetz and Dr. Zvi Dinstein entered into a shareholders agreement. In this agreement certain of our shareholders have agreed to vote their respective shares in a manner that would enable each of such shareholders to appoint a number of directors to our board of directors in proportion to each of such shareholder s holdings in our company as compared with the original holdings of all parties to this agreement. This agreement further grants each shareholder a right of first refusal to acquire the shares of a shareholder who offers his shares to a third party or a shareholder who offers more than 15% of his cumulative shareholdings (as of the date of the Israeli prospectus) in a transaction through the Tel Aviv Stock Exchange. This agreement remains in force as to a party so long as such party holds at least 25% of the number of shares in our company held by such shareholder immediately prior to our initial public offering. This agreement binds these shareholders as well as any of their assignees and transferees.

The shareholders agreement was amended in July 2002, such that Ma ariv Electronic Communications ceased to be a party to the shareholders agreement and accordingly Ma ariv Electronic Communications has no rights or obligations deriving from such agreement as of such date, including with respect to the appointment of our directors. Additionally, the mutual right of first refusal between Ma ariv Electronic Communications and the other parties to the shareholders agreement was canceled. This amendment canceled and supersedes the prior amendment to the shareholders agreement of August 2001.

As of May 31, 2003, the parties to this agreement are Dankner Investments Ltd., Mr. Hanania Gibstein, Mr. Eli Cheifetz, Mr. Shimon Cheitetz and Dr. Zvi Dinstein, and the companies controlled by such parties that hold our ordinary shares.

2. On July 30, 1998, Dankner Investments Ltd. reached an agreement with Mr. Hanania Gibstein, Mr. Shimon Cheifetz and Mr. Eli Cheifetz according to which Mr. Gibstein and Messrs. Cheifetz agreed not to sell their shares in our company without the consent of Dankner Investments Ltd. Dankner Investments Ltd. agreed not to sell its shares in our company without allowing Mr. Gibstein and Messrs. Cheifetz to take part in the sale and Mr. Gibstein and Messrs. Cheifetz agreed to join the sale of all or most of Dankner Investment s shares of our company. This agreement is subject to the Matav shareholders agreement described above.

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Significant Changes in the Ownership of Major Shareholders

Set forth below is a list of significant changes in the ownership of major shareholders for the years ended 2000, 2001 and 2002, as applicable.

1. On February 10, 2000, Dankner Investments Ltd., Ma ariv Electronic Communications, Mr. Gibstein, Messrs. Cheifetz and Dr. Dinstein concluded the following transactions in connection with our ordinary shares:

   Each of Mr. Gibstein and Messrs. Cheifetz sold 250,000 of our ordinary shares.

Each of Dankner Investments Ltd., Ma ariv Electronic Communications and Dr. Zvi Dinstein exercised their right of first refusal under the Matav shareholders agreement, and purchased the ordinary shares sold by Mr. Gibstein and Messrs. Cheifetz, in proportion to their holdings in our company, as follows:

Dankner Investments Ltd. purchased 353,914 ordinary shares;

Ma ariv Electronic Communications purchased 128,768 ordinary shares; and

Dr. Dinstein purchased 17,318 ordinary shares.

2. On May 25, 2000, Dankner Investments Ltd. acquired 48,007 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 78.58 and at an aggregate price of NIS 3,771,910.

3. On August 21, 2000, Dankner Investments Ltd. acquired 41,052 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 71.63 and at an aggregate price of NIS 2,940,555.

4. On August 22, 2000, Dankner Investments Ltd. acquired 7,455 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 72.95 and at an aggregate price of NIS 543,842 NIS.

5. On August 30, 2000, Dankner Investments Ltd. acquired 22,800 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 80.49 and at an aggregate price of NIS 1,835,172.

6. On September 27, 2000, Dankner Investments Ltd. acquired 17,000 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 83.21 and at an aggregate price of NIS 1,414,570.

7. On September 28, 2000, Dankner Investments Ltd. acquired 44,136 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 81.18 and at an aggregate price of NIS 3,582,960.

8. On October 3, 2000, Dankner Investments Ltd. acquired 1,986 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 80.48 and at an aggregate price of NIS 159,833.

9. On October 4, 2000, Dankner Investments Ltd. acquired 31,865 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 80.43 and at an aggregate price of NIS 2,562,901.

10. On October 10, 2000, Dankner Investments Ltd. acquired 12,461 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 76.28 and at an aggregate price of NIS 950,525.

11. On October 11, 2000, Dankner Investments Ltd. acquired 13,450 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 73.74 and at an aggregate price of NIS 991,803.

12. On October 12, 2000, Dankner Investments Ltd. acquired 88,000 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 67.61 and at an aggregate price of NIS 5,949,680.

13. On October 15, 2000, Dankner Investments Ltd. acquired 13,130 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 64.65 and at an aggregate price of NIS 848,855.

14. On October 16, 2000, Dankner Investments Ltd. acquired 28,419 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 66.99 and at an aggregate price of NIS 1,903,789.

15. On October 17, 2000, Dankner Investments Ltd. acquired 39,827 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 65.96 and at an aggregate price of NIS 2,626,989.

16. On October 18, 2000, Dankner Investments Ltd. acquired 69,550 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 68.75 and at an aggregate price of NIS 4,781,563.

17. On October 22, 2000, Dankner Investments Ltd. acquired 25,500 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 70.52 NIS and at an aggregate price of NIS 1,798,260.

18. On October 23, 2000, Dankner Investments Ltd. acquired 36,500 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 69.41 and at an aggregate price of NIS 2,533,465.

19. On October 24, 2000, Dankner Investments Ltd. acquired 20,289 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 68.53 and at an aggregate price of NIS 1,390,405.

20. On October 26, 2000, Dankner Investments Ltd. acquired 43,884 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 69.05 and at an aggregate price of NIS 3,030,190.

21. On October 30, 2000, Dankner Investments Ltd. acquired 21,791 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 67.06 NIS and at an aggregate price of NIS 1,461,304.

22. On October 31, 2000, Dankner Investments Ltd. acquired 11,396 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 68.02 and at an aggregate price of NIS 775,156.

23. On November 1, 2000, Dankner Investments Ltd. acquired 3,000 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 70.20 and at an aggregate price of NIS 210,600.

24. On November 5, 2000, Dankner Investments Ltd. acquired 9,197 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 72.98 and at an aggregate price of NIS 671,197.

25. On November 6, 2000, Dankner Investments Ltd. acquired 16,500 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 73.00 and at an aggregate price of NIS 1,204,500.

26. On November 7, 2000, Dankner Investments Ltd. acquired 59,449 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 72.43 and at an aggregate price of NIS 4,305,891.

27. On November 12, 2000, Dankner Investments Ltd. acquired 3,253 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 71.00 NIS and at an aggregate price of NIS 230,963.

28. On November 13, 2000, Dankner Investments Ltd. acquired 10,512 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 70.18 and at an aggregate price of NIS 737,732.

29. On November 14, 2000, Dankner Investments Ltd. acquired 3,863 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 70.00 and at an aggregate price of NIS 270,410.

30. On November 15, 2000, Dankner Investments Ltd. acquired 1,216 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 71.00 and at an aggregate price of NIS 86,336.

31. On November 16, 2000, Dankner Investments Ltd. acquired 6,259 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 70.91 and at an aggregate price of NIS 4,438,826.

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32. On November 20, 2000, Dankner Investments Ltd. acquired 44,100 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 72.75 and at an aggregate price of NIS 3,208,275.

33. On November 21, 2000, Dankner Investments Ltd. acquired 30,000 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 72.16 and at an aggregate price of NIS 2,164,800.

34. On November 22, 2000, Dankner Investments Ltd. acquired 27,500 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 71.45 and at an aggregate price of NIS 1,964,875.

35. On November 23, 2000, Dankner Investments Ltd. acquired 19,483 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 69.10 and at an aggregate price of NIS 1,346,275.

36. On November 26, 2000, Dankner Investments Ltd. acquired 6,396 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 69.10 and at an aggregate price of NIS 441,693.

37.

On November 27, 2000, Dankner Investments Ltd. acquired 2,000 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 68.50 and at an aggregate price of NIS 137,000.

38. On November 29, 2000, Dankner Investments Ltd. acquired 7,919 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 65.75 and at an aggregate price of NIS 520,674.

39. On November 30, 2000, Dankner Investments Ltd. acquired 27,947 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 67.25 and at an aggregate price of NIS 1,879,436.

40. On December 3, 2000, Dankner Investments Ltd. acquired 43,200 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 67.70 and at an aggregate price of NIS 2,924,640.

41. On December 6, 2000, Dankner Investments Ltd. acquired 12,036 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 67.43 and at an aggregate price of NIS 811,587.

42. On December 7, 2000, Dankner Investments Ltd. acquired 3,492 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 66.50 and at an aggregate price of NIS 232,218.

43. On December 10, 2000, Dankner Investments Ltd. acquired 6,094 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 66.50 and at an aggregate price of NIS 405,251.

44. On December 11, 2000, Dankner Investments Ltd. acquired 36,967 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 67.45 and at an aggregate price of NIS 2,493,424.

45. On December 12, 2000, Dankner Investments Ltd. acquired 3,624 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 66.90 and at an aggregate price of NIS 242,446.

46. On December 13, 2000, Dankner Investments Ltd. acquired 11,616 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 66.78 and at an aggregate price of NIS 775,716.

47. On December 14, 2000, Dankner Investments Ltd. acquired 6,307 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 65.70 and at an aggregate price of NIS 414,370.

48. On December 20, 2000, Dankner Investments Ltd. acquired 6,173 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 67.83 and at an aggregate price of NIS 418,715.

49. On December 21, 2000, Dankner Investments Ltd. acquired 17,668 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 68.13 and at an aggregate price of NIS 1,203,721.

50. On December 24, 2000, Dankner Investments Ltd. acquired 18,850 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 68.75 and at an aggregate price of NIS 1,295,938.

51. On December 25, 2000, Dankner Investments Ltd. acquired 10,000 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 69.07 and at an aggregate price of NIS 690,700.

52. On December 26, 2000, Dankner Investments Ltd. acquired 6,994 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 68.28 and at an aggregate price of NIS 477,550.

53. On December 27, 2000, Dankner Investments Ltd. acquired 28,833 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 68.04 and at an aggregate price of NIS 1,961,797.

54. On January 1, 2001, Dankner Investments Ltd. acquired 8,276 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 66.99 and at an aggregate price of NIS 554,409.

55. On January 7, 2001, Dankner Investments Ltd. acquired 5,805 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 65.79 and at an aggregate price of NIS 381,911.

56.

On January 8, 2001, Dankner Investments Ltd. acquired 23,200 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 65.86 and at an aggregate price of NIS 1,527,952.

57. On January 9, 2001, Dankner Investments Ltd. acquired 13,059 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 65.58 and at an aggregate price of NIS 856,409.

58. On January 11, 2001, Dankner Investments Ltd. acquired 3,886 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 64.77 and at an aggregate price of NIS 251,696.

59. On January 14, 2001, Dankner Investments Ltd. acquired 3,600 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 65.09 and at an aggregate price of NIS 234,324.

60. On January 15, 2001, Dankner Investments Ltd. acquired 20,200 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 64.49 and at an aggregate price of NIS 1,302,698.

61. On January 21, 2001, Dankner Investments Ltd. acquired 24,400 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 65.88 and at an aggregate price of NIS 1,607,472.

62. On January 22, 2001, Dankner Investments Ltd. acquired 22,570 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 64.45 and at an aggregate price of NIS 1,477,207.

63. On January 23, 2001, Dankner Investments Ltd. acquired 49,970 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 62.42 and at an aggregate price of NIS 3,119,127.

64. On January 25, 2001, Dankner Investments Ltd. acquired 11,688 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 61.35 and at an aggregate price of NIS 717,059.

65. On January 28, 2001, Dankner Investments Ltd. acquired 17,000 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 59.90 and at an aggregate price of NIS 1,018,300 NIS.

66. On January 29, 2001, Dankner Investments Ltd. acquired 24,599 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 58.58 and at an aggregate price of NIS 1,441,009.

67. On January 30, 2001, Dankner Investments Ltd. acquired 9,018 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 57.22 and at an aggregate price of NIS 516,010.

68. On February 1, 2001, Dankner Investments Ltd. acquired 26,887 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 55.24 NIS and at an aggregate price of NIS 1,505,672 NIS.

69. On February 5, 2001, Dankner Investments Ltd. acquired 15,494 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 56.00 and at an aggregate price of NIS 855,889.

70. On February 7, 2001, Dankner Investments Ltd. acquired 7,170 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 57.94 and at an aggregate price of NIS 415,430.

71. On February 12, 2001, Dankner Investments Ltd. acquired 3,985 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 57.92 and at an aggregate price of NIS 230,811.

72. On February 13, 2001, Dankner Investments Ltd. acquired 9,600 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 59.67 NIS and at an aggregate price of NIS 572,832 NIS.

73. On February 14, 2001, Dankner Investments Ltd. acquired 20,223 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 59.12 and at an aggregate price of NIS 1,195,584.

74. On February 18, 2001, Dankner Investments Ltd. acquired 6,605 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 57.27 and at an aggregate price of NIS 378,268.

75.

On February 19, 2001, Dankner Investments Ltd. acquired 3,400 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 57.54 and at an aggregate price of NIS 195,636.

76. On February 21, 2001, Dankner Investments Ltd. acquired 32,577 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 71.63 and at an aggregate price of NIS 169,726.

77. On February 22, 2001, Dankner Investments Ltd. acquired 51,000 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 71.63 and at an aggregate price of NIS 2,900,880.

78. On February 26, 2001, Dankner Investments Ltd. acquired 11,225 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 57.08 NIS and at an aggregate price of NIS 640,723.

79. On February 27, 2001, Dankner Investments Ltd. acquired 17,015 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 57.31 and at an aggregate price of NIS 975,130.

80. On September 16, 2001, Dankner Investments Ltd. acquired 6,405 ordinary shares on the Tel Aviv Stock Exchange at a price per share of NIS 27.17 and at an aggregate at a price of NIS 174,023.

On June 18, 2003 and June 19, 2003, we sold in private transactions in Israel an aggregate amount of 149,177 of our ordinary shares held by our subsidiary Cable Systems Media Haifa-Hadera Ltd., in consideration of an aggregate gross amount of approximately $1.05 million (at an average price per ordinary share of approximately $7.02). Subject to market conditions, we may in the future sell up to an additional amount of 1,194,320 of our ordinary shares held by Cable Systems Media Haifa-Hadera Ltd.

At May 31, 2003, 83,623 ADSs were held of record in the United States. These ADSs were held by 11 record holders. The number of record holders in the United States is not representative of the number of beneficial holders, nor is it representative of where such beneficial holders are resident, since many of these ADSs were held of record by brokers or other nominees.

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7B. Related Party Transactions

Subcontractor Agreement

Mr. Yehoshua Gibstein, an alternate director for Mr. Hanania Gibstein, indirectly owns 57% of Geyser Communication Services Ltd. Geyser Communication Services Ltd. owns 79% of the shares of Cabletek Ltd. In 1995, we entered into a subcontractor agreement with Cabletek Ltd. Under this agreement Cabletek Ltd. served as our subcontractor for building our network and operating our cable television services in certain communities within our franchises. For the year ended December 31, 2002, we paid Cabletek Ltd. a total of approximately NIS 2.96 million. For the period ended May 31, 2003, we paid Cabletek Ltd. a total of approximately NIS 1.11 million.

The Levit Agreement

On December 17, 1997, we entered into a bonus incentive agreement with Mr. Uri Levit (deceased), pursuant to which Mr. Levit served as vice-chairman of our board of directors until September 15, 2000. Under this agreement, Mr. Levit was entitled to receive a bonus during the period that Mr. Levit s provided service to our company, which accumulated gradually, and was calculated based on the value of our ordinary shares on the Tel-Aviv Stock Exchange. Mr. Levit was required to exercise his rights during a period of 36 months following the vesting of such rights. The exercise price per ordinary share under this right is equal to the difference between the closing price of our ordinary shares on the Tel Aviv Stock Exchange on the day of exercise and 90% of the closing price of our ordinary shares on the Tel Aviv Stock Exchange on December 17, 1997, linked to the consumer price index.

Gavish Agreement

On October 30, 2000, our audit committee and board of directors approved a bonus incentive agreement with Mr. Moshe Gavish, who served as vice chairman of our board of directors from December 31, 2000 until September 30, 2001. This agreement and amendment thereto were approved by our shareholders in its general meetings on December 31, 2000 and December 27, 2001, respectively. According to this agreement, Mr. Gavish served as active vice-chairman of our board of directors. Pursuant to this agreement, Mr. Gavish was entitled to receive a bonus that was calculated according to the value of our ordinary shares on the Tel-Aviv Stock Exchange. Under this agreement, during the period Mr. Gavish served as vice chairman of our company, Mr. Gavish was entitled to gradually accumulate a bonus, in an amount equal to a total number of our ordinary shares constituting 1% of our outstanding ordinary shares, in three equal portions at the end of 6 months, 18 months and 30 months following the beginning of his service with our company. Under the agreement, Mr. Gavish was entitled to exercise such rights during a period of 36 months following the accumulation of his rights under each portion. The exercise price for each ordinary share underlying the first portion of his right shall be an amount equal to a 17.5% discount on the difference between the closing price of our ordinary shares on the Tel-Aviv Stock Exchange on the day of the exercise, and the average price of our ordinary share on the Tel-Aviv Stock Exchange during the 30 days period prior to the approval of his agreement by our board of directors. The exercise price for each ordinary share underlying the second and third portions of his right shall be an amount equal to a 17.5% discount on the average price of our ordinary shares on the Tel-Aviv Stock Exchange during the 30 days period prior to the accumulation by Mr. Gavish of each such portion of the right. The exercise price of each ordinary share under the second and third portions of his right shall be linked to the consumer price index. The ordinary shares underlying Mr. Gavish s bonus are subject to adjustments following any distribution of bonus shares, dividend and other rights.

Upon Mr. Gavish s retirement, pursuant to the amendment to the agreement approved by the shareholders on December 27, 2001, he is entitled to receive the rights accumulated in relation to the first portion of his right (in respect of which a payment demand may be provided to us until March 15, 2004), and half of the rights in relation to the second portion of his right (in respect of which a payment demand may be provided to us until September 30, 2004). Under the amendment, the exercise price for each ordinary share underlying the rights to which he is entitled in relation to the second portion of his right shall be an amount equal to the average price of our ordinary shares on the Tel Aviv Stock Exchange during the 30 days period prior to March 15, 2002.

Investments With Shareholders

In May 2000, we decided that together with other of our shareholders, we will invest in start-up companies which engage in the fields of Internet, cable television, data communications, applications, content, infrastructure and Internet Protocol telephony.

To this end, Nonstop Ventures Ltd. was formed by several of our shareholders, in which we hold, as of November 2002, 50% of the issued share capital, following the exercise of an option granted to us under a memorandum of understanding dated December 31, 2000, as amended. Pursuant to the exercise of the said option, 50% of certain amounts we invested and loans we made on behalf of Nonstop Ventures Ltd. are deemed to be provided by us to Nonstop Ventures Ltd., in consideration of the issuance to us of a non-convertible promissory note by Nonstop Ventures Ltd., and the transfer and assignment to Nonstop Ventures Ltd. of our rights and obligations towards third parties in connection with such investments and loans. The shareholders of Nonstop Ventures Ltd. have agreed to finance its operations in proportion to their respective holdings in the share capital of Nonstop Ventures Ltd. up to a total sum of $15 million. Investments made by the respective shareholders in Nonstop Ventures Ltd. prior to October 30, 2002, are in consideration of the issuance to such shareholders of non-convertible promissory notes by Nonstop Ventures Ltd.

Since May 2000 and through May 31, 2003, we and the other shareholders have invested through Nonstop Ventures Ltd. in seven start-up companies an amount of approximately $5.8 million. Of the aggregate investment, we invested approximately $2.9 million. This amount does not include costs related to such investments such as wages, consultant fees, legal fees, etc. Due to, among other things, market factors, the financial situation of these companies and our accounting policies, these investment amounts were reduced in our financial records, and were set in our financial statements for the year ended December 31, 2001 at a value of approximately $1.4 million and were further reduced and set in our financial statements for the year ended December 31, 2002 at a value of approximately $0.6 million.

Interactive Services Agreement

In March 2001 we entered into an agreement with Connect TV Ltd., which was subsequently replaced by a memorandum of understanding dated December 25, 2002. Under these agreements Connect TV agreed to supply us with certain games and other services for our interactive television activity. Until January 2003, Dankner Investments Ltd., one of our major shareholders, held approximately 31% of the issued share capital of Connect TV, at which time Dankner Investments Ltd. sold all of its shareholdings in Connect TV. For the years ended December 31, 2001 and 2002, we have paid Connect TV approximately NIS 2.8 million and NIS 1.2 million, respectively, for services rendered.

B-Point Agreement

On May 5, 1997 we entered into two agreements with B-Point Systems Ltd., a company owned by Mr. David Binmovitch, who is the son-in-law of Mr. Shmuel Dankner. Under these agreements, B-Point Systems Ltd. provides us with cable television installation services, and sets up and maintains our cable television networks. For the year ended December 31, 2002 we paid B-Point an amount of approximately NIS 12.74 million and approximately NIS 4.66 million for the period ending May 31, 2003. The terms of these agreements have been extended by the parties and are currently in effect until June 30, 2003. Following this term we have an option to extend the terms of both agreements.

Agreement with Partner Communications Company Ltd.

On December 31, 2002, we entered into an agreement with Partner Communications Company Ltd. (or Partner), a company in which Mr. Shmuel Dankner and Mr. Dor Dankner are directors on behalf of us. The agreement provides for SMS messaging between our cable television network and Partner s cellular mobile network by and between our subscribers and the subscribers of Partner.

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Payment to Mr. Dor Danker

On October 31, 2002, our shareholders resolved to approve a payment of $50,000 to Mr. Dor Dankner, a member of our board of directors, for his services over the years since 1998 on our behalf in connection with Partner Communications Company Ltd., including, among other things, with regard to the sale of approximately half of our holdings in Partner Communications Company Ltd. during April 2002.

Payment to Dankner Investments Ltd.

On May 21, 2003, our audit committee and board of directors resolved to approve in principle a payment of $600,000 to Dankner Investments Ltd., our controlling shareholder, for the efforts of its executives on our behalf in connection with the proposed merger of the Israeli cable television operators. This payment is subject to the approval of our shareholders and will be presented to our shareholders for approval at the next general meeting.

7C. Interests of Experts and Counsel

Not applicable.

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ITEM 8. FINANCIAL INFORMATION

8A. Consolidated Statements and Other Financial Information

Audited financial statements for the three fiscal years ended December 31, 2002are included at Item 18. Financial Statements.

Legal and Arbitration Proceedings

In addition to the legal proceedings discussed below, we are a party to a number of legal and administrative proceedings arising in the ordinary course of our business. We do not expect the outcome of such matters in the aggregate to have a material adverse effect upon our business and financial condition, results of operations and cash flows.

(a) On September 8, 1998, a lawsuit was filed in the Tel-Aviv-Jaffa District Court against us and other cable television operators. The suit alleges that we, together with the other cable television operators, performed certain acts in purchasing the rights to broadcast the Spanish soccer league games, resulting in a breach of an agreement between the parties, and consequently, that we were unjustly enriched in an amount constituting the difference between the price which we actually paid to purchase the rights to broadcast and the price we were prepared to pay prior to signing the agreement. The plaintiff seeks, among other things, compensation in an aggregate amount of adjusted NIS 30.4 million, which for the purposes of court fees was limited to NIS 7.6 million. Together with the other cable television operators, we submitted a statement of defense. The parties submitted their affidavits. The parties notified the Court that they consent to a mediation procedure, and currently the parties are required to notify the Court the identity of the mediator.

(b) On April 22, 1999, a lawsuit and application to recognize the suit as a class action were filed in the Tel-Aviv-Jaffa District Court against us. The suit alleges that we constitute a monopoly, and that we adversely exploit our position in the market, in a manner which is, or may be, damaging to the general public, among other things, by setting and collecting an unreasonable and unfair price for the services we provide. The plaintiff is seeking, among other things, that we be required to reduce the subscriber fees we collect and to pay our subscribers compensation in connection with the subscriber fees we collected from May 10, 1996 through April 1, 1999. In this context, the plaintiff claims he has sustained damages in an amount of NIS 1,279, and the sum of compensation due to all of the members of the class in the action, if certified as a class action, amounts to approximately NIS 332 million (subject to adjustment). The plaintiff is further claiming compensation for alleged damages caused to all of the members of the class in the action, if certified as a class action, from the date of filing the lawsuit up to the date judgment is rendered. We opposed the action being certified as a class action, claiming that the motion lacks any material substance, on grounds that the plaintiff disregarded the high investments we made in infrastructure and equipment, that the franchise we were granted for cable television broadcasts is limited in time, the comparisons made by the plaintiff between our company and foreign companies dealing in cable television broadcasts in countries where the situation is very different are not relevant to our modus operandi, and finally because the subscriber fees we charge are subject to supervision and highly regulated. Before a hearing on the merits of the action shall be held, a preliminary hearing was held to decide matters of law raised by us, which, if accepted by the Court, would result in a ruling to dismiss the suit. If the Court does not rule in our favor with respect to the preliminary issues, a hearing on the merits of the application to recognize the suit as a class action will be held. On February 28, 2002, all parties submitted submissions regarding the preliminary issues. A hearing has been scheduled for August 11, 2003 for the delivery of judgment by the Court with respect to the preliminary issues.

(c) On November 8, 1999, the Commissioner of Restrictive Business Practices, declared us to be a monopoly in the field of providing multi-channel television broadcasts for payment, in the regions in which we operate. On December 28, 1999, we filed an appeal against this determination with the Restrictive Business Practices Court. In our appeal, we claim, among other things, that the Commissioner s declaration should be revoked (i) due to lack of due process, including, among other things, that the declaration lacks an appropriate factual foundation, and (ii) on merit, due to the fact that in the relevant market we do not provide over 50% of the services in our license areas in which we operate and therefore we are not a monopoly in this market. The Commissioner counter-claimed our appeal, requesting that it be dismissed, together with appeals filed by the other cable television operators on the same issues. The Restrictive Trade Practices Court concluded the deposition stage of the appeal on October 30, 2001, and the parties have submitted their summaries to the Court. The parties are currently waiting for the ruling of the Restrictive Business Practices Court on this appeal**.**

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(d) On November 14, 1999, a lawsuit and application to recognize the suit as a class action were filed in the Haifa District Court against us and our subsidiary, Cable System Media Haifa-Hadera Ltd. The suit alleges that we, together with our subsidiary, constitute a monopoly, and that we adversely exploit our position in the market to collect unreasonable and unfair subscriber fees. The plaintiff is seeking, among other things, that we repay her subscriber fees in the amount of NIS 2,258, and that we compensate all of the members of the class in the action, if certified as a class action, in an amount of approximately NIS 528 million (subject to adjustment). At our request, the Israeli Supreme Court ordered the transfer of this lawsuit to the Tel-Aviv-Jaffa District Court, so that it may be adjudicated together with the lawsuit filed on April 22, 1999 (paragraph (b) above), as our defense is based on the same grounds and both claims are closely related. We, together with our subsidiary, filed a response opposing the confirmation of the claim as a class action on the grounds that the claim disregards the high investments made in infrastructure and equipment which have yet to be recovered; that the franchise granted to us for cable television broadcasts is limited in time; and that the claim possesses no factual basis and is not supported by expert opinion. The District Court has issued a temporary stay of action pending resolution of the preliminary hearing of the lawsuit filed on April 22, 1999 (paragraph (b) above).

(e) On March 28, 2000, a claim was filed in the Tel-Aviv-Jaffa District Court against the cable television operators, including our company, by the Association for the International Collective Management of Audiovisual Works AGICOA, or AGICOA, an international association of producers of cinema and television works. The aggregate sum of the claim is not less than approximately $171 million and for the purpose of court fees was limited to an initial sum of $20 million. AGICOA claim that the cable television operators infringed the AGICOA s copyright in broadcasting of programs, without its permission and payment of consideration. The AGICOA is also claiming unjust enrichment on the part of the cable television operators and that they be ordered to submit their accounts. In our statement of defense, filed on July 9, 2000, we claim, among other things, that AGICOA have no right to file this claim in light of the restrictive business practices laws in Israel. The dispute was transferred by the Court to mediation in the second quarter of 2001. The mediation was not successful and the matter was returned to the Court. At a preliminary hearing held on June 18, 2002, the Court ruled to delay its decision in this matter pending resolution of the Israeli Supreme Court in a further hearing in another matter, which the Court believes will have material implications on all or part of this dispute. However, the Court determined that the preliminary proceedings in this dispute may be commenced and completed. At the parties consent, the Court deferred the completion of the preliminary proceedings to the months of October - December 2003. A date for the hearing will be set following completion of the preliminary proceedings.

The further hearing referred to by the Court was filed with respect to the ruling of the Supremes Court residing as an appellate court, which determined that the transmission of broadcasts as secondary broadcasts may also constitute an infringement of copyrights, if such broadcasts include copyrights owned by third parties who have not consented to their broadcast in Israel. AGICOA s motion to be included as a party to the proceedings was denied by the Supreme Court. On October 27, 2002, the parties to the further hearing completed the submission of their pleadings to the Supreme Court.

(f) On August 21, 2000, a lawsuit and application to recognize the suit as a class action were filed in the Haifa District Court against us. The suit, filed by six plaintiffs, residents of Arab and Druse villages in the Hadera district, alleged that contrary to the provisions of our previous franchise, we did not complete the connection of all the residents residing within our license area to our cable television network by mid-1996. The plaintiffs sought, among other things, a mandatory injunction forcing us to connect their villages to our cable television network; and that we pay the residents of these villages compensation for the time period they were not connected. The plaintiff s claim for compensation was based on the subscriber fees we collect from our subscribers, at an amount of NIS 171 per subscriber each month. The lawsuit claimed to represent 10,981 residents in these areas, so the aggregate sum claimed was approximately NIS 72.5 million, plus NIS 2.1 million for each additional month from the date the suit was filed through the date on which these homes were connected to our cable television network. In our defense we denied the suitability of this suit being adjudicated as a class action as the class of persons and the merits of the claim failed to meet the legal requirements of such action. On August 27, 2002, the Court denied the application to recognize the lawsuit as a class action.

(g) In September 2000, a claim was filed in the Tel-Aviv-Jaffa Labor Court against our company by a plaintiff who claims that an employer-employee relations existed between him and our company and that as a consequence, our company is required to pay him the amount of an adjusted NIS 2.6 million in respect of severance pay and other salary components. In parallel, in September 2000, our company and its subsidiary, Cable Systems Media Haifa-Hadera Ltd., filed a monetary claim with the Netanya Magistrates Court in an amount of adjusted NIS 1 million contending that the plaintiff violated, in a basic and severe manner, undertakings to deliver an advanced telemarketing system to our company and its subsidiary. This claim was transferred to mediation by the Netanya Magistrates Court, which was not successful. On November 15, 2001, the Netanya Magistrates Court issued a resolution joining the above two claims to be heard in the Tel-Aviv Jaffa District Labor Court. The parties affidavits have been submitted to the Court and a preliminary hearing has been set for July 15, 2003. To date, a date has not been set for the hearing.

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(h) On December 31, 2001, the Commissioner of Restrictive Trade Practices petitioned the Restrictive Trade Practices Court to order a number of companies, including ourselves, to invest approximately $2.5 million in local productions. Together with the above petition, an unopposed petition was also submitted, pursuant to which the companies will invest the aforementioned sum over the period ending in mid-2004, subject to the decision of the Restrictive Trade Practices Court on the principal petition. It has been decided that, should the Restrictive Trade Practices Court rule that the companies are not required to make this investment, then the amount already invested by the companies will be set off against the amounts that they are required to invest in local productions in the future. A procedural agreement has been endorsed by the Court stipulating that the Court shall first rule upon the preliminary matter of the obligation to invest. On February 18, 2003, the Court ruled that the respective companies (which include Noga Communications 1995 Ltd.) are required to make this investment, in an amount to be determined by the Court. To date, a date has not been set for the hearing to determine the amount to be invested by the respective parties.

(i) In May 2002, D.B.S. Satellite Services (1998) Ltd., or YES, and Bezeq, - Israeli Telecommunications Corporation Ltd., or Bezeq, filed appeals in the Restrictive Trade Practices Court against the decision of the Commissioner of Restrictive Trade Practices for the approval to the proposed merger of the Israeli cable television operators. Bezeq subsequently requested to cancel its appeal. The cable television operators and the Commissioner requested the Court to determine that Bezeq be obligated to pay expenses. To date, the Court has not ruled on the matter of such expenses. YES requests in its appeal to cancel the merger approval, based on its claim that the merger between the cable television operators harms competition in the field of multi-channel television, and alternatively requests to change the terms of the approval such that, among other things, a corporate separation of the merged entities shall be required, the exclusive purchase of content shall be prohibited and the mutual sale obligation requirement shall be terminated. The parties summaries were heard by the Court. To date, the Court has not ruled on this matter.

(j) On December 3, 2002, a lawsuit and application to recognize the suit as a class action were filed in the Tel Aviv - Jaffa District Court against us, the other Israeli cable television operators, the Council and the Ministry. The suit, filed by seven plaintiffs, alleges that we and the other cable television operators violated the terms of the approval of the Council for the transmission of the pay sport channel (offered to subscribers through the tiering services) since we and the other cable television operators did not maintain certain programs in the original sport channel which is part of the basic packages offered to subscribers. The lawsuit is claimed to represent 1,050,000 subscribers. The plaintiffs are seeking that we and the other cable television operators pay compensation to all of the members of the class in the action, if certified as a class action, in a total amount of approximately NIS 302,400,000 as of the date of the motion, plus NIS 25,200,000 for each additional month from the date the suit was filed up to the date judgment is rendered by the Court. In accordance with the suit, our portion of the claimed compensation is approximately 26% of the alleged aggregate amounts. A response to the application was submitted to the Court on behalf of all of the respondents. In our response, we opposed the action being certified as a class action on grounds that the class of persons of the claim fail to meet the legal requirements of such an action, and that the cable television operators and the original cable sport channel producer have complied with most of the terms of the Council s approval. The hearing for the application to recognize the suit as a class action has been scheduled for October 26, 2003.

(k) On August 28, 2002, a lawsuit and application to recognize the suit as a class action were filed in the Tel Aviv - Jaffa District Court against us and the other Israeli cable television operators. The suit, filed by three plaintiffs, alleges that we and the other cable television operators did not connect the members of the class in the action, if certified as a class action, to cable television services up to the date the suit was filed. The plaintiffs are seeking that we and the other cable television operators pay compensation to all of the members of the class in the action, if certified as a class action. In accordance with the suit, our portion of the claimed compensation is approximately NIS 139,420,000. We and one of the other cable television operators, Golden Channels &Co. (or Arutzi Zahav), filed a motion to dismiss the suit without prejudice, due to the dismissal of a lawsuit identical in substance to this suit (paragraph (f) above). The Court determined that the motion for dismissal of the suit without prejudice will be heard together with the application to recognize the suit as a class action. We and Arutzi Zahav &

Co. filed a response to the application to recognize the suit as a class action. The hearing for the application to recognize the suit as a class action has been suspended due to the stay of proceedings to which Tevel Israel International Ltd. (one of the other cable television operators) is subject.

(l) On November 27, 2002, the cable television operators, including us, filed a petition in the Israeli Supreme Court of Justice against the Minister of Communications, the Minister of Finance and the Economics Committee of the Israeli parliament, due to the refusal of the Economic Committee to approve the proposed amendments to regulations promulgated under the Telecommunications Law, regarding a gradual reduction in the royalties payable by Cable Broadcast Licensees under the Cable Broadcast Licenses. In the petition, we and the other cable television operators claim that this refusal discriminates against us in the field of multi channel broadcast in relation to D.B.S. Satellite Services (1998) Ltd., or YES , that is obligated to pay lower royalty rates. In our petition, we and the other cable television operators request that the royalties we are obligated to pay be equal to those proposed by the Minister of Communications in the proposed amendments, and further request that the Minister of Finance be instructed to return to us, in respect of royalties paid as of January 1, 2002 and pending resolution of the petition, an amount equal to the difference between 5% of the cable television operators revenues derived from multi channel broadcasts and the amount that would be payable in accordance with the proposed amendments (pursuant to the policy of the Ministries of Communications and Finance). In its response, the State of Israel claims that the petition is premature, as the Economics Committee has not yet ruled on this matter and has postponed the date of the vote on this matter. In a response to the State s response, the cable television operators opposed the State s claims. In a hearing held on March 20, 2003, the Court notified the State representative that the State s preliminary response to the petition is not acceptable to the Court and the Court issued an order instructing the State to provide the Court within 45 days reasons why the Court should not accept the claims of the cable television operators. On June 16, 2003, the Economic Committee of the Israeli parliament resolved to approve the Minister of Communications proposed amendment to regulations promulgated under the Telecommunications Law and to reduce the royalties payable by Cable Broadcast Licensees as proposed, in a manner that corresponds with the royalty rates that YES is obligated to pay under law. Following the official publication of the said approved amendment, we intend to file a motion to dismiss the petition.

(m) On October 16, 2001, Play.T.V. Ltd. and Mr. Yair Hasson, the producers of the Playboy channel, filed a petition in the Israeli Supreme Court of Justice against the Israeli parliament and the Minister of Communications. The plaintiffs request the Israeli Supreme Court of Justice to issue an order whereby the amendment to the Telecommunications Law regarding certain restrictions of broadcast of a channel that broadcasts are mostly sexual broadcasts, is void, and alternatively, the Court is requested to rule that the amendment will become effective in 4 years or at a later date. The Council, the cable television operators, including us, and D.B.S. Satellite Services (1998) Ltd., or YES, are formal respondents to the petition. On March 3, 2002, the State of Israel submitted a response to the Court on behalf of the Israeli parliament, the Minister and the Council. In its response, the State opposed the plaintiffs requests and included a motion for dismissal of the petition without prejudice. On July 16, 2002, the plaintiffs filed a motion to amend the petition, pursuant to further amendments to the Telecommunications Law, under which broadcasts that include abominable material in the meaning of the Israeli Penal Law, 1977, and which include certain content as set forth in the Telecommunications Law, is prohibited as of August 2002. The Council was requested by the Supreme Court to determine its policy in connection with the implementation of the aforesaid latter amendment to the Telecommunications Law. Following the latter amendment, the cable television operators and YES submitted to the Council a request for the approval of the transmission of the Playboy channel, based on the claim that the Playboy channel broadcasts are not contrary to the law, which was subsequently rejected by the Council on November 28, 2002. On March 25, 2003, the Supreme Court determined that an extended constitution of court of 11 Supreme Court judges will rule on the petition, on the basis of the summaries previously submitted by the parties to the Court, however the parties will be entitled to complete their claims. To date, a date has not been set for a hearing. In May 2003, the Israeli cable television operators submitted a request to the Council to reconsider its position regarding the broadcast of the Playboy channel, due to the change of certain circumstances. On June 12, 2003, the Council determined that when taking into account all the relevant interests, following the latter amendment to the Telecommunications Law, this Law should be interpreted such that the broadcasts of the Playboy channel shall not be deemed to be restricted broadcasts as defined under this Law, and therefore resolved that the Playboy channel may be broadcast, subject to certain conditions and limitations. Such conditions and limitations stipulate that, among other things, the Playboy channel will be transmitted only at certain stipulated times and offered to digital subscribers as a separate pay channel and not as part of the digital Basic Package; Cable Broadcast Licensees are required to take reasonable measures to ensure that the channel shall be purchased only by subscribers over the age of 18; the channel will be coded such that access will be available only by a personal code; and Cable Broadcast Licensees are required to transmit during the transmission of the channel certain broadcasts regarding the prohibition on exposure of children and youth to the channel. To date, the petitioners have not notified the Supreme Court regarding the above development.

(n) On June 17, 2003, following the Council s decision of June 12, 2003, that permits the broadcast of the Playboy channel, subject to certain conditions and limitations (paragraph (m) above), certain social organizations filed in the Israeli Supreme Court of Justice a petition against the Council, the Chairman of the Council, Play.T.V. Ltd., the Israeli cable television operators (including us) and D.B.S. Satellite Services (1998) Ltd., or YES , requesting all of the respondents to explain why the said decision of the Council should not be cancelled and why the Chairman of the Council should not be prevented from participating and voting in the discussions regarding the Playboy channel due to prejudice. Additionally, the petitioners filed a motion for an interim injunction to prevent the commencement of the broadcast of the Playboy channel pending the ruling of the Supreme Court on this petition. On June 18, 2003, the Supreme Court denied the motion for an interim injunction and determined that an extended constitution of court of 3 Supreme Court judges will hear the petition as soon as possible. On June 26, 2003 a hearing was held in the Supreme Court. The Supreme Court determined that that this petition will be heard together with the petition of the Chairperson of the Advancement of Women´s Status Committee of the Israeli parliament and 37 other Israeli parliament members (paragraph (o) below) by an extended constitution of court of Supreme Court judges, which shall be determined by the President of the Supreme Court. The Supreme Court issued an order determining that the respondents are to explain why the decision of the Council to approve the broadcast of the Playboy channel should not be cancelled, and why the Chairman of the Council should not be prevented from participating and voting in the discussions regarding the Playboy channel due to prejudice. The respondents are to submit their response within 45 days, and the petitioners are to submit 30 days thereafter their response to the respondents´ response. The Supreme Court denied the motion for an interim injunction to prevent the commencement of the broadcast of the Playboy channel pending the ruling of the Supreme Court on this petition.

(o) On June 18, 2003, the Chairperson of the Advancement of Women s Status Committee of the Israeli parliament and 37 other Israeli parliament members, filed in the Israeli Supreme Court of Justice against the Council, Play.T.V. Ltd., the Israeli cable television operators (including us) and D.B.S. Satellite Services (1998) Ltd., or YES , a petition for an order nisi, directed towards the Council, to explain why the Council should not retract its decision to approve the broadcast of the Playboy channel, as such decision was unlawfully approved, is contrary to the Telecommunications Law, contrary to its prior decision and contrary to proper administration laws. Additionally, the petitioners filed a motion for an interim injunction, which, with respect to the Council, shall prevent the Council from executing its decision, and, with respect to the other respondents, shall prevent the public broadcast of the Playboy channel, pending the ruling of the Supreme Court on this petition. On June 26, 2003 a hearing was held in the Supreme Court. The Supreme Court determined that that this petition will be heard together with the petition of the certain social organizations (paragraph (n) above) by an extended constitution of court of Supreme Court judges, which shall be determined by the President of the Supreme Court. The Supreme Court issued an order determining that the respondents are to explain why the decision of the Council to approve the broadcast of the Playboy channel should not be cancelled, and why the Chairman of the Council should not be prevented from participating and voting in the discussions regarding the Playboy channel due to prejudice. The respondents are to submit their response within 45 days, and the petitioners are to submit 30 days thereafter their response to the respondents´ response. The Supreme Court denied the motion for an interim injunction to prevent the commencement of the broadcast of the Playboy channel pending the ruling of the Supreme Court on this petition.

(p) Warner Bros. International Television Distribution (or Warner Bros.), a provider of movie and series content broadcasted on the family and movie channels of the Israeli cable television operators, including ours, recently filed two lawsuits in the District Court of Los Angeles, California, United States, against the two other Israeli cable television operators, Tevel Israel International Ltd. (or Tevel) and the Golden Channel & Co. (or Arutzi Zahav). These suits allege that these cable television operators are in breach of their respective license agreements with Warner Bros. Warner Bros. seeks, among other things, compensation in an amount of not less than $17 million (Tevel) and $16 million (Arutzi Zahav), and a declaratory judgment of cancellation of the respective license agreements. Warner Bros. also filed a motion in each of the suits for a preliminary injunction regarding the broadcast of movie and series content provided by Warner Bros. to each of the cable television operators. On March 31, 2003, the District Court of Los Angeles denied the preliminary injunction motion filed in connection with the suit against Arutzi Zahav. The Arutzi Zahav lawsuit is being heard at the District Court of Los Angeles.

Tevel is subject to a stay of proceedings in Israel, currently valid until July 2, 2003, and the Trustee appointed for the duration of the stay of proceedings filed a motion in the Tel Aviv District Court to determine that for the duration of the stay of proceedings, it is not possible to hold legal proceedings against Tevel in the United States. On February 16, 2003, the Tel Aviv District Court accepted the Trustee s position and determined that the law suit filed in the California Court was unlawfully filed, due to, among other things, the stay of proceedings to which Tevel is subject. The Tel Aviv District Court determined, among other things, that the suit filed by Warner Bros. in California shall have no effect and will not be enforceable in Israel, and further determined with respect to the use by Tevel of the movie content provided to Tevel according to the license agreement, that in the absence of a valid injunction issued by a competent court, Tevel is not prevented from reasonably using such content, subject to applicable law. On March 13, 2002, Warner Bros. filed an appeal in the Israeli Supreme Court (and, for reasons of caution, a motion to leave to appeal) against this decision of the Tel Aviv District Court. On March 25, 2003, the Trustee denied most of Warner Bros. demand for payment of alleged debt. On April 24, 2003, Warner Bros. filed in the Tel Aviv District Court an appeal to this decision of the Trustee, and Warner Bros. was subsequently requested to file an amended appeal. On May 12, 2003, a hearing was held in the District Court of Los Angeles, in which it was agreed that the parties will submit their positions to the Court regarding such Court s authority to continue the proceedings and a hearing was scheduled for this matter for June 30, 2003. On June 12, 2003, the Trustee filed a motion in the Tel Aviv District Court, which includes a motion for a stay of the proceedings held in the District Court of Los Angeles pending resolution of the appeal filed by Warner Bros. in the Israeli Supreme Court against the decision of the Tel Aviv District Court. On June 18, 2003, Warner Bros. filed its repose to the said motion. In accordance with the decision of the Tel Aviv District Court dated June 26, 2003, the Trustee is to submit its response to Warner Bros.´s response to the motion within five days.

(q) On March 30, 2003, the State of Israel (through the representatives of the Attorney General of the Ministry of Trade of Commerce) filed an indictment in the Netanya Magistrate Court against us, Mr. Amit Levin, our Chief Executive Officer and Mr. Doron Admati, our marketing and programming manager at the time relevant to the indictment, for the offense of Prohibition to Mislead Consumers Regarding a Material Issue in a Transaction according to the Consumer s Protection Law, 1981. In accordance with the indictment, the defendants are alleged to have misled consumers within the framework of a certain publication published in connection with a certain sales promotion campaign. To date, the indictment has only been served to Mr. Doron Admati. To date, a hearing has not been scheduled for the reading of the indictment and the defendant s responses to the indictment.

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Dividend Distribution Policy

We have not adopted any dividend distribution policy and we cannot assure that we would pay additional dividends in the future. In the past we have distributed cash dividends. See Item 3A. Key Information Selected Financial Data - Payment of Dividends to Shareholders.

8B. Significant Changes

No significant change has occurred since the date of our financial statements.

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ITEM 9. THE OFFER AND LISTING

9A. Offer and Listing Details

Our share capital consists of ordinary shares, which have been listed for trading on the Tel Aviv Stock Exchange since October 1993 and ADSs, which have been listed for quotation on the Nasdaq National Market since June 12, 1996, under the symbol MATV . Each ADS represents two ordinary shares.

The tables below set forth, for the periods indicated, the high and low closing market prices for our ordinary shares and ADSs, as reported by the Tel Aviv Stock Exchange and the Nasdaq National Market, respectively.

		Nasdaq ($ per ADS)		Nasdaq (NIS per ADS)		Tel Aviv Stock Exchange ($ per ordinary share)		Tel Aviv Stock Exchange (NIS per ordinary share)	
		High	**Low**	**High**	**Low**	**High**	**Low**	**High**	**Low**
Most recent five full financial years									
1998		26.75	16.87	97.86	60.40	13.61	8.14	49.80	29.00
1999		59.00	19.87	245.02	80.17	28.51	9.95	120.40	41.40
2000		69.25	32.81	281.57	132.69	34.59	15.70	141.90	64.69
2001		34.25	9.74	140.70	38.45	17.02	5.22	69.90	22.75
2002		18.58	8.34	83.11	42.19	9.20	4.27	40.82	20.58
Most recent two full financial years									
2001									
	First Quarter	34.25	17.75	140.70	73.25	17.02	8.78	69.90	36.23
	Second Quarter	22.07	15.12	91.57	63.19	11.15	7.60	46.26	31.78
	Third Quarter	17.30	10.80	75.61	38.45	10.60	5.22	44.89	22.75
	Fourth Quarter	21.55	9.74	91.29	42.43	8.83	5.41	38.71	23.13
2002									
	First Quarter	18.58	11.70	83.11	54.69	9.20	5.80	40.82	27.06
	Second Quarter	12.05	8.84	57.67	143.60	6.13	4.49	29.36	22.10

Third Quarter	11.40	9.66	54.88	46.26	5.64	4.98	26.27	23.18
Fourth Quarter	11.03	8.34	51.48	42.19	6.13	4.27	28.60	20.58
Most recent six months								
December 2002	12.30	10.44	57.40	49.79	6.13	5.24	28.60	24.85
January 2003	11.57	9.91	55.18	48.43	5.82	4.96	28.00	24.22
February 2003	11.98	10.10	57.62	49.37	5.87	5.05	28.51	24.66
March 2003	12.10	10.72	56.19	51.98	6.06	5.52	28.38	26.75
April 2003	15.70	11.76	71.65	54.78	7.65	6.00	35.02	27.90
May 2003	14.78	12.56	66.27	57.21	7.46	6.29	33.30	28.79

9B. Plan of Distribution

Not applicable.

9C. Markets

Our ADSs are quoted on the Nasdaq National Market under the symbol MATV and our ordinary shares are traded on the Tel Aviv Stock Exchange.

9D. Selling Shareholders

Not applicable.

9E. Dilution

Not applicable.

9F. Expenses of the Issue

Not applicable.

ITEM 10. ADDITIONAL INFORMATION

10A. Share Capital

Not applicable.

10B. Memorandum and Articles of Association

Purposes and Objects of the Company

We are a public company registered under the Israeli Companies Law as Matav Cable Systems Media Ltd., registration number 52-004007-2.

Pursuant to our memorandum of association, we were formed mainly for the purpose of establishing television and cable television networks, broadcasting and to provide such services and related and ancillary services in Israel and without derogating from the above, we are also empowered to hold any right, obligation or legal action and to operate in any business or matter approved by our company.

Pursuant to our articles of association, our board of directors is entitled to donate reasonable amounts to worthy causes, up to a limited sum.

The Powers of the Directors

The power of our directors to vote on a proposal, arrangement or contract in which the director is materially interested is limited by the relevant provisions of the Companies Law. In addition, the power of our directors to vote compensation to themselves or any members of their body requires the approval of the audit committee and the shareholders at a general meeting. For information regarding approval of related party transactions and fiduciary duties of directors, see Item 6C. Directors, Senior Management and Employees - Board Practices Approval of Related Party Transactions.

Subject to applicable laws, the powers of our directors to borrow are not limited, except in the same manner as any other transaction by the company.

Our articles do not limit the age of retirement of our directors.

Directors in our company are not required to hold shares for director qualification.

Rights Attached to Shares

Our registered share capital consists of a single class of 100 million ordinary shares, par value NIS 1.00 per share, of which 30,203,917 ordinary shares were issued and outstanding as of December 31, 2002, and May 31, 2003. All outstanding ordinary shares are validly issued, fully paid and non-assessable. The rights attached to the ordinary shares are as follows:

Dividend rights

Under our articles of association, holders of our ordinary shares are entitled to the full amount of any cash or share dividend subsequently declared. Our board of directors may propose a dividend with respect to any fiscal year out of profits in accordance with the provisions of the Companies Law. For additional information regarding Israeli tax consequences, see Item 10E. Additional Information Taxation.

Seven years after a dividend has been declared and is still unclaimed, the person so entitled to it is deemed to have waived his or her right to receive such dividend and such amount is returned to our company. We are not obligated to pay interest or linkage on an unclaimed dividend.

Voting rights

With the exception of 1,194,320 of our ordinary shares held by Cable Systems Media Haifa-Hadera Ltd. as at June 20, 2003 (which do not carry voting rights for so long as they are held by Cable Systems Media Haifa-Hadera Ltd., or any of our subsidiaries, in accordance with the Israeli Companies Law), under our articles of association, holders of our ordinary shares have one vote for each ordinary share held on all matters submitted to a vote of shareholders. Such voting rights may be affected by the grant of special voting rights to the holders of a class of shares with preferential rights that may be authorized in the future. The quorum required for an ordinary meeting of shareholders consists of at least two shareholders present or by proxies who hold or represent, in the aggregate, at least 40% of the voting rights of the issued share capital. In the event that a quorum is not present within 30 minutes of the scheduled time, the shareholders meeting will be adjourned to the same day of the following week, at the same time and place, or such time and place as the board of directors may determine. If at such reconvened meeting a quorum is not present within half an hour of the time fixed for the meeting any two shareholders present in person or by proxy or in any other manner permitted by the Companies Law will constitute a quorum.

Under the Companies Law, unless otherwise provided in the articles of association or applicable law, all resolutions of the shareholders require approval by the holders, in a general meeting, of a majority of the voting rights represented at the meeting, in person or by proxy, and voting on the matter. Under our articles of association a special majority is required to approve a change of rights attached to a certain class of shares or to cancel a class of shares. See Item 10B. Additional Information - Memorandum and Articles of Association - Changing Rights Attached to Shares .

Under our articles of association, our directors are appointed by a simple majority of our shareholders at a general meeting, duly convened, and they serve until the next annual meeting or until earlier termination of their office pursuant to our articles of association, provided that, outside directors shall be elected in accordance with applicable law and/or relevant stock exchange rules applicable to us. For information regarding the appointment of outside directors, see Item 6C. Directors, Senior Management and Employees - Board Practices Independent Directors and Outside Directors. In each annual general meeting the directors that were elected at the previous annual general meeting are deemed to have resigned from their office. A resigning director may be reelected. However, our directors are nominated according to the provisions of a shareholders agreement from October 1993, as more fully described in Item 7A. Major Shareholders and Related Party Transactions Major Shareholders - Matav Shareholders Agreement.

According to our articles of association each ordinary share represents one vote. The ordinary shares do not have cumulative voting rights in the election of directors.

Currently, our articles of association provide that a majority of our board of directors, entitled to participate, may appoint additional directors, up to the maximum number permitted.

Rights in the Company s profits

Our shareholders have the rights to share in our profits distributed as a dividend and any other permitted distribution. See Item 10B. Additional Information - Rights Attached to Shares Dividend Rights.

Rights in the event of liquidation

All of our ordinary shares confer equal rights among them with respect to amounts distributed to shareholders in case of liquidation.

Changing Rights Attached to Shares

In order to change the rights attached to our shares, the general meeting of the shareholders must adopt a resolution to change such rights by a majority of the votes of shareholders participating in the meeting and voting on the matter. However, if our share capital is divided into different classes of shares, in order to change the rights attached to a certain class of shares or cancel a certain class of shares, our articles of association require the approval of a special majority representing at least 75% of the votes of the shareholders participating in the general meeting and voting on the matter, provided that the holders of such class of shares have consented to such action by unanimous written consent or by a special majority representing at least 75% of the holders of such class of shares participating in a class meeting and voting on the matter (unless the terms of such class of shares provide otherwise).

Annual and Special Meetings

According to the Israeli Companies law, our board of directors must convene an annual meeting of shareholders at least once every calendar year, within 15 months of the last annual meeting. Notice of at least 21 days prior to the date of the annual meeting is required. A special meeting may be convened by the board of directors, as it decides or upon a demand of any two directors or 25% of the presiding directors, or of one or more shareholders holding in the aggregate at least 5% of our issued capital and 1% of our voting rights, or of one or more shareholders holding in the aggregate at least 5% of our voting rights. A special meeting must be held not more than 35 days from the publication date of the announcement of the meeting.

Anti-Takeover Provisions; Mergers and Acquisitions

Our Cable Broadcast Licenses, Infrastructure License and HeadEnd License include restrictions regarding changes of means of control of the Licensees. See Item 4B. Information on the Company Business Overview Our Licenses - Restrictions Upon Changes of Means of Control . In accordance with the Cable Broadcast Licenses, the restrictions set forth in these Licenses regarding changes of means of control of the Licensees have been entrenched in our articles of association, as approved by our shareholders at the annual general meeting of October 31, 2002.

The Israeli Companies Law allows for mergers, provided that each party to the transaction obtains the approval of its board of directors and shareholders. For the purpose of the shareholder vote of each party, unless a court rules otherwise, a statutory merger will not be deemed approved if a majority of the shares of one party to the merger which are not held by the other party to the potential merger (or by any person who holds 25% or more of the shares of the other party to the potential merger, or the right to appoint 25% or more of the directors of the other party to the potential merger) have voted against the merger. Upon the request of a creditor of either party to the proposed merger, the court may delay or prevent the merger if the court concludes that there exists a reasonable concern that as a result of the merger the surviving company will be unable to satisfy the obligations of such party. Finally, a merger may not be completed unless at least 70 days have passed from the time that the requisite proposals for approval of the merger were filed with the Israeli Registrar of Companies.

In addition, provisions of the Companies Law that address arrangements between a company and its shareholders allow for squeeze-out transactions in which a target company becomes a wholly-owned subsidiary of an acquiror. These provisions generally require that the merger be approved by a majority of the participating shareholders holding at least 75% of the shares voted on the matter. In addition to shareholder approval, court approval of the transaction is required, which entails further delay. The Companies Law also provides for a merger between Israeli companies after completion of the above procedure for an arrangement transaction and court approval of the merger.

The Companies Law also provides that an acquisition of shares in a public company must be made by means of a tender offer if, as a result of such acquisition, the purchaser would become a 25% shareholder of the company. This rule does not apply if there is already another 25% shareholder of the company. Similarly, the Companies Law provides that an acquisition of shares in a public company must be made by means of a tender offer if, as a result of the acquisition, the purchaser would become a 45% shareholder of the company, unless there is already a majority shareholder of the company. The Israeli Minister of Justice has the authority to adopt regulations exempting from these tender offer requirements companies that are publicly traded outside of Israel, such as us. In any event, if as a result of an acquisition of shares a purchaser would hold more than 90% of a company s shares, the acquisition must be made by means of a tender offer for all of the company s shares. If more than 95% of the outstanding shares are tendered in the tender offer, all shares that the purchaser offered to acquire are transferred to such purchaser.

Israeli tax law treats stock-for-stock acquisitions between an Israeli company and another company less favorably than does U.S. tax law. For example, Israeli tax law may, under certain circumstances, subject a shareholder who exchanges his ordinary shares for shares of another corporation to taxation prior to the sale of the shares received in such stock-for-stock swap.

Changes in Our Capital

Changes in our capital are subject to the approval of the shareholders at a general meeting by a majority of the votes of shareholders participating in the general meeting and voting on the matter.

10C. Material Contracts

Except for agreements listed below, we are not a party to any material contracts other than those entered into in the ordinary course of business.

Arrangements in connection with the proposed merger of the Israeli cable television operators. For information, see Item 4B. Information on the Company - Business Overview - Agreement for a Merger of the Cable Television Operators .

10D. Exchange Controls

There are no Israeli government laws, decrees or regulations that restrict or that affect our export or import of capital or the remittance of dividends, interest or other payments to non-resident holders of our securities, including the availability of cash and cash equivalents for use by us and our wholly owned subsidiaries, except or otherwise as set forth under Item 10E. Additional Information Taxation.

Under Israeli law, persons who are neither residents nor nationals of Israel may freely hold, vote and transfer ordinary shares in the same manner as Israeli residents or nationals.

Neither our articles of association nor our memorandum of association contain any restrictions on non-residents or non-nationals of Israel concerning the holding, voting or transfer of our ordinary shares.

10E. Taxation

The following is a summary of the current tax laws of the State of Israel as they relate to us and our shareholders. The following also includes a discussion of the material Israeli tax consequences to persons purchasing our ordinary shares. To the extent that the discussion is based on legislation yet to be subject to judicial or administrative interpretation, there can be no assurance that the views expressed herein will accord with any such interpretation in the future. This discussion is not intended and should not be construed as legal or professional tax advice and does not cover all possible tax considerations.

Tax Reform

On January 1, 2003, the Law for Amendment of the Income Tax Ordinance (Amendment No. 132), 5762-2002, known as the Tax Reform, came into effect.

The Tax Reform, aimed at broadening the categories of taxable income and reducing the tax rates imposed on employment income, introduced the following, among other things:

Reduction of the tax rate levied on real capital gains (other than gains deriving from the sale of listed securities) derived after January 1, 2003, to a general rate of 25% for both individuals and corporations. Regarding assets acquired prior to January 1, 2003, the reduced tax rate will apply to a proportionate part of the gain, in accordance with the holding periods of the asset, before or after January 1, 2003, on a linear basis;

Imposition of Israeli tax on all income of Israeli residents, individuals and corporations, regardless of the territorial source of income, mainly on a personal basis, including income derived from passive sources such as interest, dividends and royalties;

Introduction of controlled foreign corporation (CFC) rules into the Israeli tax structure. Generally, under such rules, an Israeli resident who holds, directly or indirectly, 10% or more of the rights in a foreign corporation whose shares are not publicly traded (or which has offered less than 30% of its shares or any rights to its shares to the public), in which more than 50% of the rights are held directly or indirectly by Israeli residents, and a majority of whose income or profits in a tax year is considered passive income, will be liable for tax on the portion of such income attributed to his holdings in such corporation, as if such income were distributed to him as a dividend;

Imposition of capital gains tax on capital gains realized by individuals as of January 1, 2003, from the sale of shares of companies publicly traded on the Tel Aviv Stock Exchange (such gain was previously exempt from capital gains tax in Israel in certain circumstances). For information with respect to the applicability of Israeli capital gains taxes on the sale of our ordinary shares, see Capital Gains Tax below;

Introduction of a new regime for the taxation of shares and options issued to employees and officers (including directors); and

Introduction of tax at a rate of 25% on dividends paid by one Israeli company to another (which are generally not subject to tax), if the source of such dividend is income that was derived outside of Israel (provided that such income was not subjected to corporate tax).

General Corporate Tax Structure

Israeli companies are generally subject to income tax at the corporate tax rate of 36% and are generally subject to capital gains tax at a rate of 25% for capital gains derived after January 1, 2003 (excluding assets which were acquired before the Reform and sold after).

Taxation Under Inflationary Conditions

The Income Tax (Inflationary Adjustment) Law 1985 (the Inflationary Adjustments Law), attempts to overcome some of the problems presented to a traditional tax system by rapid inflation. Generally, the Inflationary Adjustments Law provides tax deductions and adjustments to depreciation deductions and tax loss carry forwards to mitigate the effects resulting from an inflationary economy. Our taxable income is determined under this law.

Dividends

We currently do not intend to pay dividends for the foreseeable future. See Item 8A. Financial Information Consolidated Statements and Other Financial Information Dividend Distribution Policy. However, the following Israeli tax consequences would apply in the event we actually pay any dividends in respect of ordinary shares.

Taxation of Israeli Residents

The distributions of dividends, other than bonus shares (stock dividends), are generally subject to income tax at a rate of 25% (that is withheld at source) for individuals. Distribution of dividends, other than bonus shares, to Israeli corporations are subject to a tax at a rate of 25% (that is withheld at source) if the source of such dividends is income derived outside of Israel and are exempt from tax if the source of such dividends is income derived in Israel. See Item 10E. Additional Information—Taxation—Capital Gains Tax Taxation of Israeli Residents.

Taxation of Non-Israeli Residents

Non-residents of Israel are subject to income tax on income accrued or derived from sources in Israel, including dividends from Israeli corporations. Distributions of dividends other than bonus shares (stock dividends) are subject to income tax at a rate of 25% that is withheld at source, unless a different rate is provided in a treaty between Israel and the shareholder s country of residence.

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Capital Gains Tax

General

Israeli law generally imposes a capital gains tax on the sale of capital assets located in Israel or the sale of direct or indirect rights to assets located in Israel, including on the sale of shares in Israeli companies by both residents and non-residents of Israel, unless a specific exemption is available or unless a tax treaty between Israel and the shareholder country of residence provides otherwise. The law distinguishes between Real Gain and Inflationary Surplus . Real Gain is the excess of the total capital gain over Inflationary Surplus computed on the basis of the increase in the Israeli consumer price index between the date of purchase and the date of sale. Real Gains (other than gains deriving from the sale of listed securities) derived after January 1, 2003 are taxed at a rate of 25% for both individuals and corporations

Taxation of Israeli Residents

Pursuant to the Tax Reform, generally, capital gains tax is imposed at a rate of 15% on real gains derived on or after January 1, 2003, from the sale of shares in companies (i) publicly traded on the Tel Aviv Stock Exchange (TASE) or; (ii) (subject to a necessary determination by the Israeli Minister of Finance) Israeli companies publicly traded on a recognized stock exchange outside of Israel (such as us). This tax rate is contingent upon the shareholder not claiming a deduction for financing expenses (in which case the capital gain will be taxed at a rate of 25%) and does not apply to: (i) dealers in securities (who will be taxed at a rate of 36% for corporations and at a marginal tax rate of up to 50% for individuals); (ii) shareholders that report in accordance with the Inflationary Adjustment Law (who will be taxed at a rate of 36% for corporations and at a marginal tax rate of up to 50% for individuals); or (iii) shareholders who acquired their shares prior to an initial public offering (that are subject to a different tax arrangement). The tax basis of shares acquired prior to January 1, 2003 will be determined in accordance with the average closing share price in the three trading days preceding January 1, 2003. However, a request may be made to the tax authorities to consider the actual adjusted cost of the shares as the tax basis if it is higher than such average price.

Taxation of Non-Israeli Residents

Non-Israeli residents are exempt from Israeli capital gains tax on any gains derived from the sale of shares publicly traded on the TASE, and are exempt from Israeli capital gains tax on any gains derived from the sale of shares of Israeli companies publicly traded on a recognized stock exchange or regulated market outside of Israel, provided that such capital gains are not derived from a permanent establishment in Israel and that such shareholders are not subject to the Inflationary Adjustment Law and did not acquire their shares prior to an initial public offering. However, non-Israeli corporations will not be entitled to such exemption if an Israeli resident (i) has a controlling interest of 25% or more in such non-Israeli corporation, or (ii) is the beneficiary of or is entitled to 25% or more of the revenues or profits of such non-Israeli corporation, whether directly or indirectly.

In some instances where our shareholders may be liable to Israeli tax on the sale of their ordinary shares, the payment of the consideration may be subject to the withholding of Israeli tax at the source.

Taxation of Residents of the United States under the U.S. Treaty

Residents of the United States generally will be subject to withholding tax in Israel deducted from dividends paid, if any, on the ordinary shares. Generally, under the Convention between the Government of the United States and the Government of the State of Israel with respect to Taxes on Income (referred to as the US Treaty), the maximum withholding tax on dividends paid to a holder of ordinary shares or ADSs who is a resident of the United States (as defined in the US Treaty) will be 25% (and if such shareholder is a U.S. corporation holding at least 10% of the issued voting stock through out the tax year in which the dividend is distributed as well as the previous tax year then, the maximum tax on dividend is 12.5%). The US Treaty exempts from taxation in Israel any capital gain realized on the sale, exchange or other disposition of ordinary shares or ADSs by a holder that is a resident of the United States for purposes of the US Treaty, and that owns directly or indirectly, less than 10% of our voting stock at all times during the 12-month period preceding such sale, exchange or other disposition.

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Sellers of ordinary shares, who are residents of the United States and who hold 10% or more of the outstanding ordinary shares at any time during such 12-month period will be subject to Israeli Capital Gains Tax. However, under the US treaty, residents of the United States (as defined in the US Treaty) would be permitted to claim a credit for this tax against U.S. federal income tax imposed on the sale, exchange or other disposition, subject to the limitations in U.S. laws applicable to foreign tax credits. The US treaty does not relate to U.S. state or local taxes.

United States Information Reporting and Backup Withholding

Dividend payments made to holders, and proceeds paid from the sale, exchange, or disposal of ordinary shares may be subject to information reporting to the Internal Revenue Service and possible US federal backup withholding at a rate of 30% in 2002 and 28% as of 2003 and thereafter. Certain exempt recipients (such as corporations) are not subject to these information reporting requirements. Backup withholding will not apply to a holder who furnishes a correct taxpayer identification number or certificate of foreign status and makes any other required certification, or who is otherwise exempt from backup withholding. Any US persons required to establish their exempt status generally must file Internal Revenue Service Form W-9 (Request for Taxpayer Identification Number and Certification). Non-US holders generally will not be subject to US information reporting or backup withholding. However, such holders may be required to provide certification of non-US status in connection with payments received in the United States or through certain US-related financial intermediaries. Finalized Treasury regulations have generally expanded the circumstances under which US information reporting and backup withholding may apply.

Backup withholding is not an additional tax. Amounts withheld as backup withholding may be credited against a holder s US federal income tax liability. A holder may obtain a refund of any excess amounts withheld under the backup withholding rules by filing the appropriate claim for refund with the Internal Revenue Service and furnishing any required information.

Repatriation

Non residents of Israel who acquire any of our ADSs using non Israeli currencies will be able to repatriate dividends, liquidation distributions and the proceeds from the sale of such ADSs, into non Israeli currencies at the rate of exchange prevailing at the time of repatriation provided that any applicable Israeli income tax has been paid, or withheld, on such amounts if applicable.

United States Federal Income Tax Considerations

Subject to the limitations described in the next paragraph, the following discussion describes the material United States federal income tax consequences to a holder of ordinary shares, referred to for purposes of this discussion as a U.S. holder, that is:

a citizen or resident of the United States;

a corporation created or organized in the United States or under the laws of the United States or of any state;

an estate, the income of which is includible in gross income for United States federal income tax purposes regardless of its source; or

a trust, if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more U.S. persons have the authority to control all substantial decisions of the trust.

In addition, certain material aspects of United States federal income tax relevant to a holder other than a U.S. holder, referred to as a Non-U.S. holder, are discussed below.

This summary is for general information purposes only. It does not purport to be a comprehensive description of all of the tax considerations that may be relevant to each person s decision to purchase ordinary shares.

This discussion is based on current provisions of the Internal Revenue Code of 1986, as amended, United States Treasury Regulations promulgated there under and administrative and judicial interpretations thereof, all as in effect as of the date of this Annual Report on Form 20-F, all of which are subject to change, possibly on a retroactive basis. This discussion does not address all aspects of United States federal income taxation that may be relevant to any particular shareholder based on such shareholder s individual circumstances. In particular, this discussion considers only U.S. holders that will own ordinary shares as capital assets and does not address the potential application of the alternative minimum tax or United States federal income tax consequences to U.S. holders that are subject to special treatment, including U.S. holders that:

are broker-dealers or insurance companies;

have elected mark-to-marketing accounting;

are tax-exempt organizations;

are financial institutions or financial services entities ;

hold ADSs or ordinary shares as part of a straddle, hedge or conversion transaction with other investments;

own directly, indirectly or by attribution at least 10% of the Company s outstanding voting shares;

acquire their shares in a compensatory transaction; or

have a functional currency that is not the dollar.

In addition, this discussion does not address any aspect of state, local or non-United States tax laws.

Additionally, the discussion does not consider the tax treatment of persons who hold ADSs or ordinary shares through a partnership or other pass-through entity or the possible application of United States federal gift or estate tax. Material aspects of United States federal income tax relevant to a holder other than a U.S. holder are also discussed below.

Each holder of ADSs or ordinary shares is advised to consult such person s own tax advisor with respect to the specific tax consequences to such person of purchasing, holding or disposing of the Company s ADSs or ordinary shares.

Taxation of Dividends Paid on Ordinary Shares

Unless a distribution constitutes qualified dividend income, a U.S. holder will be required to include in gross income as ordinary income the amount of any distribution paid on ordinary shares, including any Israeli taxes withheld from the amount paid, on the date the distribution is received to the extent the distribution is paid out of the Company s current or accumulated earnings and profits as determined for United States federal income tax purposes. Distributions in excess of these earnings and profits will be applied against and will reduce the U.S. holder s basis in the ordinary shares and, to the extent in excess of such basis, will be treated as gain from the sale or exchange of ordinary shares.

Dividends paid on the ordinary shares to a non-corporate U.S. holder in taxable years beginning after December 31, 2002 and before January 1, 2009, are taxable to the U.S. holder at a maximum tax rate of 15% provided that the shares or ADSs are held by the U.S. holder for more than 60 days during the 120-day period beginning 60 days before the ex-dividend date. Such dividends are referred to as qualified dividend income. The dividend will not be included in qualified dividend income, however, to the extent that the U.S. holder is under an obligation (whether pursuant to a short sale or otherwise) to make related payments with respect to positions in substantially similar or related property. In addition, the dividend will not be included in qualified dividend income if the Company was a foreign investment company, a passive foreign investment company, or a foreign personal holding company in either the taxable year of the distribution or the preceding year.

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Credit for Israeli Taxes Withheld

U.S. holders will have the option of claiming the amount of any Israeli income taxes withheld at source either as a deduction from gross income or as a dollar-for-dollar credit against their United States federal income tax liability. Individuals who do not claim itemized deductions, but instead utilize the standard deduction, may not claim a deduction for the amount of the Israeli income taxes withheld, but such amount may be claimed as a credit against the individual s United States federal income tax liability. The amount of foreign income taxes which may be claimed as a credit in any year is subject to complex limitations and restrictions, which must generally be determined on an individual basis by each shareholder. The limitations set out in the Code include, among others, rules which limit foreign tax credits allowable with respect to specific classes of income to the United States federal income taxes otherwise payable with respect to each such class of income. Distributions of current or accumulated earnings and profits will be foreign source passive income for United States foreign tax credit purposes and will not qualify for the dividends received deduction available to corporations. The total amount of allowable foreign tax credits in any year cannot exceed regular U.S. tax liability for the year attributable to foreign source taxable income. However, a U.S. holder who is a natural person may elect not to be subject to the foreign tax credit limitation rules if all of that U.S. holder s foreign source income is qualified passive income and his or her creditable foreign taxes do not exceed $300, or $600 for joint returns, in a taxable year. Qualified passive income includes dividends and other amounts, but only to the extent the U.S. holder receives a Form 1099 or similar payee statement with respect to that qualified passive income. A U.S. holder will be denied a foreign tax credit with respect to Israeli income tax withheld from dividends received on the ordinary shares to the extent such U.S. holder has not held the ordinary shares for at least 16 days of the 30-day period beginning on the date which is 15 days before the ex-dividend date or to the extent such U.S. holder is under an obligation to make related payments with respect to substantially similar or related property. Any days during which a U.S. holder has substantially diminished its risk of loss on the ordinary shares are not counted toward meeting the 16-day holding period required by the statute. Special rules apply in determining the foreign tax credit limitation with respect to qualified dividend income that is subject to the maximum 15% tax rate.

Taxation of the Disposition of Ordinary Shares

Upon the sale, exchange or other disposition of ordinary shares, a U.S. holder will generally recognize capital gain or loss in an amount equal to the difference between such U.S. holder s basis in the ordinary shares, which is usually the cost of such shares, and the amount realized on the disposition. Capital gain from the sale, exchange or other disposition of ordinary shares held more than one year is generally long-term capital gain and, if recognized on or after May 6, 2003 and before January 1, 2009, is generally taxed to individual U.S. holders at a maximum rate of 15% (reduced from the 20% maximum rate that applied to long-term capital gain recognized before May 6, 2003). Gains and losses recognized by a U.S. holder on a sale, exchange or other disposition of ordinary shares will generally be treated as United States source income or loss for United States foreign tax credit purposes. The deductibility of a capital loss recognized on the sale, exchange or other disposition of ordinary shares is subject to limitations.

Tax Consequences if the Company is a Passive Foreign Investment Company

The Company will be a passive foreign investment company, or PFIC, if 75% or more of its gross income in a taxable year, including the pro rata share of the gross income of any company, U.S. or foreign, in which the Company is considered to own 25% or more of the shares by value, is passive income. Alternatively, the Company will be considered to be a PFIC if at least 50% of the average value of its gross assets in a taxable year calculated quarterly and ordinarily determined based on fair market value, including the pro rata share of the assets of any company in which the Company is considered to own 25% or more of the shares by value are held for the production of, or produce, passive income. For this purpose, passive income includes dividends, interest, royalties, rents, annuities and the excess of gain over losses from the disposition of assets which produced passive income. If the Company were a PFIC, and a U.S. holder did not make an election to treat the Company as a qualified electing fund (as described below), then:

excess distributions by the Company to a U.S. holder would be taxed in a special way. Excess distributions are amounts received by a U.S. holder with respect to the Company s shares or ADSs in any taxable year that exceed 125% of the average distributions received by that U.S. holder from the Company in (i) the three previous years or (ii) the U.S. holder s holding period for ordinary shares before the present taxable year, if shorter. Excess distributions must be allocated ratably to each day that a U.S. holder has held the Company s securities. A U.S. holder must include amounts allocated to the current taxable year in its gross income as ordinary income for that year. A U.S. holder must pay tax on amounts allocated to each prior taxable year at the highest rate in effect for that year on ordinary income and the tax is subject to an interest charge at the rate applicable to deficiencies for income tax.

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the entire amount of gain that was realized by a U.S. holder upon the sale or other disposition of ordinary shares will also be rated as an excess distribution and will be subject to tax as described above.

a U.S. holder s tax basis in the Company s shares that were acquired from a decedent would not receive a step-up to fair market value as of the date of the decedent s death but would instead be equal to the decedent s basis, if lower.

The special PFIC rules described above will not apply to a U.S. holder if the U.S. holder makes an election to treat the Company as a qualified electing fund, or QEF, in the first taxable year in which the U.S. holder owns ordinary shares. Instead, a shareholder of a qualified electing fund is required for each taxable year to include in income a pro rata share of the ordinary earnings of the qualified electing fund as ordinary income and a pro rata share of the net capital gain of the qualified electing fund as long-term capital gain, subject to a separate election to defer payment of taxes, which deferral is subject to an interest charge. A U.S. holder may make a QEF election only if the Company agrees to furnish the U.S. holder annually with certain tax information on a PFIC annual information statement. The Company does not presently prepare or provide such information, and such information may not be available to U.S. holders if the Company is subsequently determined to be a PFIC.

A U.S. holder of PFIC stock which is publicly traded could elect to make an election to mark-to-market the ordinary shares annually, rather than be subject to the above-described rules. Under such election, the U.S. holder will include as ordinary income or loss each year an amount equal to the difference as of the close of the taxable year between the fair market value of the PFIC stock and the holder s adjusted basis in the PFIC stock. Losses would be allowed only to the extent of net mark-to-market gain previously included by the U.S. holder under the election for prior taxable years. If the mark-to-market election were made, then the rules set forth above would not apply for periods covered by the election.

The Company believes that it was not a PFIC in 2002. However, the tests for determining PFIC status are applied annually and it is difficult to make accurate predictions of future income and assets, which are relevant to this determination. Accordingly, there can be no assurance that the Company will not become a PFIC.

U.S. holders who hold ordinary shares or ADSs during a period when the Company is a PFIC will be subject to the foregoing rules, even if the Company ceases to be a PFIC, subject to certain exceptions for U.S. holders who made a QEF or mark-to-market election. A U.S. holder who beneficially owns shares in a PFIC must file an annual return with the IRS on IRS Form 8621 that describes any distributions received with respect to such shares and any gain realized on the disposition of such shares.

U.S. holders are urged to consult their tax advisors about the PFIC rules, including the consequences to them of making a mark-to-market or QEF election with respect to the Company s ordinary shares and ADSs in the event that the Company qualifies as a PFIC.

Tax Consequences for Non-U.S. Holders of Ordinary Shares

Except as described in Information Reporting and Back-up Withholding below, a Non-U.S. holder of ADSs or ordinary shares will not be subject to U.S. federal income or withholding tax on the payment of dividends on, and the proceeds from the disposition of, ordinary shares, unless:

such item is effectively connected with the conduct by the Non-U.S. holder of a trade or business in the United States and, in the case of a resident of a country which has a treaty with the United States, such item is attributable to a permanent establishment or, in the case of an individual, a fixed place of business in the United States;

the Non-U.S. holder is an individual who holds ADSs or the ordinary shares as a capital asset and is present in the United States for 183 days or more in the taxable year of the disposition and does not qualify for an exemption; or

the Non-U.S. holder is subject to tax pursuant to the provisions of United States tax law applicable to U.S. expatriates.

Information Reporting and Backup Withholding

U.S. holders generally are subject to information reporting requirements with respect to dividends paid in the United States on ADSs or ordinary shares. U.S. holders are also generally subject to back-up withholding on dividends paid in the United States on ordinary shares unless the U.S. holder provides IRS Form W-9 or otherwise establishes an exemption. U.S. holders are subject to information reporting and back-up withholding at a rate of up to 28% on proceeds paid from the disposition of ADSs or ordinary shares unless the U.S. holder provides IRS Form W-9 or otherwise establishes an exemption.

Non-U.S. holders generally are not subject to information reporting or back-up withholding with respect to dividends paid on, or upon the disposition of, ADSs or ordinary shares, provided that the non-U.S. holder provides a taxpayer identification number, certifies to its foreign status, or otherwise establishes an exemption.

The amount of any back-up withholding will be allowed as a credit against a U.S. or Non-U.S. holder s United States federal income tax liability and may entitle such holder to a refund, provided that certain required information is furnished to the IRS.

10F. Dividends and Paying Agents

Not applicable.

10G. Statement by Experts

Not applicable.

10H. Documents on Display

Reports and other information of ours filed with the Securities and Exchange Commission can be inspected without charge and copied at prescribed rates at the public reference facilities maintained by the Securities and Exchange Commission at 450 Fifth Avenue, N.W., Washington, D.C. 20549, and at the regional offices of the Securities and Exchange Commission located at Seven World Trade Center, Suite 1300, New York, New York 10048 and the Northwest Atrium Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661-2511.

Copies of this material are also available by mail from the Public Reference Branch of the Securities and Exchange Commission, at 450 Fifth Street, N.W., Washington, D.C. 20549, at prescribed rates.

10I. Subsidiary Information

Not applicable.

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ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

General

We are exposed to risks deriving from changes in the exchange rate of the shekel against foreign currencies, to risks deriving from changes in the interest rates and inflation rates, and to other market risks. From time to time, we examine the exposure and the risks that such exposures create, and take hedging measures, while taking market conditions into consideration. However, there is no assurance that our hedging measures will offset, either in whole or in part, if at all, the financial effects deriving from adverse changes in exchange rates, interest rates, inflation rates or other market risks. We do not hold or issue hedging instruments for the purpose of trading in them. See Note 15 of our financial statements.

Risks Deriving from Exchange Rates

As at December 31, 2002, we had liabilities denominated or linked to foreign currency in an aggregate amount of approximately NIS 72 million, and assets denominated or linked to foreign currency in an aggregate amount of approximately NIS 6.8 million. Substantially all of our programming expenses, certain other expenses, and some of our capital expenditures, are denominated or linked to foreign currency (which, for the year ended December 31, 2002 was NIS 135.2 million). On the other hand, all of our revenue (which, for the year ended December 31, 2002, was NIS 505 million) is wholly denominated in shekels.

Subsequent to the balance sheet date, in light of the fluctuation in the exchange rate of the U.S. dollar in relation to the NIS during 2002, we entered into derivative transactions to purchase U.S. dollars at predetermined exchange rates (forward transactions). As a result of the matter described above, we recorded a financial loss in our financial statements for the first quarter of 2003 in the amount of about NIS 1.8 million.

Risks Deriving from Inflation

Our financial expenses are affected by, among other things, the inflation rate in Israel. High rates of inflation cause a decrease in the real value of our unlinked assets, which in turn, causes an increase in our financial expenses. Likewise, high rates of inflation cause a decrease in the real value of our unlinked liabilities, which in turn, causes a decrease in our financial expenses.

Regarding our assets and liabilities that are linked to the Israeli consumer price index and unlinked, see Note 15 of our financial statements.

Further, we may be unable to update the fees we collect from our subscribers in order to keep pace with inflation, due to regulatory restrictions and/or market factors. This may cause a decrease of our income in real terms.

Risks Deriving from Interest Rates

In addition to the exchange rate exposure, as described above, we have short term loans bearing variable interest rates, which are linked to the prime interest rate, determined by the Bank of Israel which is the standard interest rate for inter-bank loans. Since we present our financial statements in real terms, we are exposed to the change in the Israeli consumer price index on our interest expenses of short-term bank loans. The long-term loans, including debentures which we have issued, are mainly linked to the Israeli consumer price index plus a fixed interest percentage above the Israeli consumer price index, and some are linked to the US dollar plus a fixed interest percentage above the LIBOR. See, Item 18. Financial Statements Notes to Consolidated Financial Statements . We do not hedge any of our risks deriving from interest rates.

Other Market Risks

Our operations may be affected, among other things, by legislative and regulatory changes, regulatory policy, technological changes and changes in the behavior of our customers, particularly as a result of competition in the telecommunications services market, in general, and the multi-channel television market, in particular.

ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

Not applicable.

PART II

ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

None

ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS

Material Modifications to the Rights of Security Holders

At our annual general shareholders meeting held on October 31, 2002, our shareholders resolved to amend our articles of association to include restrictions regarding changes of means of control of Matav, as required and set forth in our Cable Broadcast Licenses. For information, see Item 4B. Information on the Company Business Overview Our Licenses - Restrictions Upon Changes of Means of Control .

Use of Proceeds

None

ITEM 15. CONTROLS AND PROCEDURES

Within 90 days prior to the date of this annual report, we carried out an evaluation, under the supervision and with the participation of our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures are effective to ensure that information required to be included in our periodic reports to the Securities and Exchange Commission is recorded, processed, summarized and reported in a timely manner.

In addition, there have been no significant changes in our internal controls or in other factors that could significantly affect those controls subsequent to the date of their last evaluation.

Although we believe our pre-existing disclosure controls and procedures and internal controls were adequate to enable us to comply with our disclosure obligations, as a result of such review we intend to implement changes, primarily to formalize and document procedures already in place.

ITEM 16. [RESERVED]

PART III

ITEM 17. FINANCIAL STATEMENTS

We have responded to Item 18. Financial Statements in lieu of responding to this Item.

ITEM 18. FINANCIAL STATEMENTS

The following financial statements are filed as part of this annual report.

INDEX TO FINANCIAL STATEMENTS

ITEM 19. EXHIBITS

The exhibits filed with or incorporated by reference into this annual report are listed on the index of exhibits below.

Exhibit Number	Description
1.1	Matav s Articles of Association, as adopted on December 31, 2000 and amended on October 31, 2002
*1.2	English translation of Matav s Memorandum of Association
*2(a)	Specimen Certificate for American Depository Shares
3.1	English translation of Shareholders Agreement dated October 18, 1993
3.2	English translation of Amendment to Shareholders Agreement dated October 18, 1993, dated July 8, 2002
**4(a)(i)-A	English summary of Merger Arrangement dated December 31, 2001
4(a)(i)-B	English summary of final version of Merger Agreement dated February 2003
4 (b)(ii)(b)-A	English translation of Cable Broadcast License dated April 30, 2002, as amended, granted to Matav- Cable Systems Media Ltd., and Cable Broadcast License dated April 30 2002, as amended, granted to Matav - Cable Systems Media Haifa - Hadera Ltd.
4(b)(ii)(b)-B	English translation of Telecommunications Infrastructure License dated March 27, 2002 granted to Matav Infrastructure 2001 L.P.
**4(b)(ii)(b)-C	English summary of Broadcasting HeadEnd License dated May 2, 2002 granted to Cable Systems Media Haifa - Hadera Ltd.
4(c)	English translation of 2001 Senior Employee Option Plan

6	See Note 2(m) to our financial statements for information explaining how net loss per share information was calculated
8	List of Subsidiaries
10.1	Consent of Kost, Forer and Gabay
99.1	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
99.2	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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* Incorporated herein by reference to our registration statement on Form F-1 (No. 333-4822).

** Incorporated herein by reference to Matav s Annual Report on Form 20-F for the fiscal year ending December 31, 2001.

The terms of the Cable Broadcast License granted to Matav Cable Systems Media Haifa - Hadera Ltd. are substantially identical to the terms of the Cable Broadcast License granted to Matav Cable Systems Media Ltd. In accordance with Rule 12b-31, only the latter is exhibited hereto (Exhibit 4 (b)(ii)(b)-A). The only substantial differences between the two licenses are in relation to fees and license areas. An English translation of the annexes of the licenses relating to these issues is exhibited hereto separately for each license.

GLOSSARY OF SELECTED TERMS

The following explanations are not intended as technical definitions, but to assist the reader to understand certain terms as used in this annual report.

GLOSSARY

ADSL:asymmetric digital subscriber line, refers to a modem technology that provides enhanced and affordable access to the Internet, video streaming, and a wide variety of other multimedia broadband services over existing copper twisted-pair wire-lines. The ADSL is the basic and most commonly used technology (of the DSL family) offered by telecommunication companies.

Broadband: a general term used to describe wide bandwidth equipment or networks which carry large amounts of analog and digital information over a frequency spectrum. A broadband cable television and telecommunications network can deliver multiple channels and other services.

Buildout: refers to the process of digging, laying cable, filling, and covering underground trenches in the streets which pass by the homes and installing and connecting the necessary electronic equipment in a license area.

Cable television: refers to a cable television network which employs transmission over coaxial and/or fiber-optic cable to transmit multiple channels carrying images, sound and data, between a central facility and an individual subscriber s television set. Networks may allow one-way or two-way transmission from a HeadEnd to a subscriber with a return path to the HeadEnd.

Cable television operator: refers to the entity which has been granted a Cable Broadcast License, by the Ministry of Communications pursuant to its authority under regulations promulgated within the scope of the Telecommunications Law, for the purpose of providing cable television services for a specific license area, building and operating a cable television network. The current cable television operators previously operated under exclusive franchises granted by the Ministry of Communications.

Churn: refers to the discontinuance of cable television services to a subscriber either, voluntarily or involuntarily, and commonly measured as a rate from period to period. Subscribers who disconnect and simultaneously reconnect are not included as having disconnected for purposes of calculating the churn rate.

Churn rate: refers to cable television subscriber termination rates expressed by calculating the total number of disconnected cable television subscribers during the relevant period as a percentage of the average number of cable television subscribers during that period.

Coaxial cable: refers to a cable consisting of a central conductor surrounded by and insulated from another conductor. It is the standard material used in traditional cable television networks. Signals are transmitted through this cable at different frequencies, giving a channel capacity greater than the capacity of a twisted pair cable, but smaller than the capacity of a fiber-optic cable.

Council: refers to the Israeli Council for Cable and Satellite Broadcasting.

Dish: refers to an antenna shaped like a dish used to receive television signals from a satellite.

DBS: refers to direct broadcasting satellite services.

Download: refers to the transfer of information from the network to a computer, such as games or music files.

Downstream Path:refers to a broad-band (85-860MHz), One-to-Many HFC network segment, which carries RF signals (TV Channels) from the network HeadEnd, Down to all the subscribers homes. (Very basic, One-Way Cable services utilize the downstream path only).

DSL:digital subscriber line, refers to a modem technology that provides enhanced and affordable access to the Internet, video streaming, and a wide variety of other multimedia broadband services over existing copper twisted-pair wire-lines; DSL operates with different data rates in the two directions. The ADSL is part of the DSL technology family.

EPG Services: refers to electronic program guide services and broadcasting.

Fiber-optic cable: refers to a cable made of glass fibers through which signals are transmitted as a light energy. This cable is capable of carrying a large number of channels and other data and telecommunications information.

GSM: refers to the global system for mobile communications. This system is a comprehensive digital standard for the operation of all elements of a cellular telephone system. GSM originated in Europe, but is now the most popular digital mobile telephone standard used worldwide.

HeadEndrefers to a collection of hardware, typically including, satellite dishes, satellite receivers, modulators, amplifiers and videocassette playback machines. After being processed, signals are then combined for distribution within the cable television network.

High Speed Internet over cable: refers to High Speed Internet access over cable broadband infrastructure, through the use of a cable modem and personal computer.

Homes passed: is an expression in common usage and referring to the measurement of the size of a cabled area, meaning the total number of premises which have the potential of becoming connected to a cable television network. A home is deemed passed if it can be connected to the cable television distribution network without further extension of trunk transmission lines.

Inside Wiring: refers to a part of the public telecommunications network that is located in the premises of the subscriber, and is designed to serve the premises of only such subscriber

Interactive services: refers to different services by way of interactive applications that are provided to our digital subscribers through the use of the subscriber s digital set-top box, such as Games Channels, Horoscopes, Weather and Classifieds.

LMDS: refers to local multipoint distribution system, which is a point to multipoint service with a two-way capability to transmit voice, data and video information. LMDS offers innovative consumer services such as two way interactive video, advanced teleconferencing, telemedicine, telecommuting and high-speed data services.

Minister: refers to the Israeli Minister of Communications

Off-air TV: refers to over-the-air broadcast television channels that are available to viewers in Israel free of charge. Currently, such channels are the Israel Broadcast Authority (Channel 1 and 33), the Middle East Channel, the commercial channels (Channel 2 and 10), the general Russian Channel and other off-air channels, which broadcast from other selected countries.

Pay-Per-View: refers to the payment made for individual cable television films or events on per program basis.

Penetration: refers to the measurement of the take-up of cable television services. Penetration is calculated by dividing the total number of subscribers by the total number of homes passed.

PMB: plastic media blast. Refers to plastic granules used for paint and surface cleaning in the electronic industries, aircraft, space and defense maintenance industries as well as in the chemical, glass, plastic, rubber and food industries.

PVR: personal video recorder. Refers to a device, based on large storage (hard-drive) and an easy-to-use user interface, which enables digital smart recording/playback of video content. PVR can also be used as a limited substitute to video on demand (or VOD) services (while the content is pre-loaded in advance and watched by the user later-on). PVRs can either be embedded within a digital set-top box or function as a stand-alone device.

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SMATV: satellite master antenna television systems. Refers to a television program delivery system to multiple dwelling units utilizing satellite transmissions.

Subscriber: refers to a subscriber to a cable television distribution system for cable television services.

Set-top box:refers to an auxiliary device that usually rests on top of or adjacent to a television receiver. The set-top box is used to receive analog or digital transmissions and digital television to be viewed on an ordinary television set. The set-top device may convert television or signals to a form or format that allows end-user channel selection or interaction. It may tune channels that the television does not tune and may include descrambling circuitry. It may also include an electronic program guide.

Standard fiber optic links:refers to broadband communication link which utilizes fiber optic transmission technology.

Telecommunications Law: refers to the Israeli Telecommunications Law (Telecommunications and Broadcasting), 1982, as amended, and the rules and regulations promulgated thereunder by the Ministry of Communications and the Council for Cable and Satellite Broadcasting. The Telecommunications Law governs the licensing and operation of the telecommunications industry in the State of Israel.

Telephony: refers to the provision of telephone services.

Terminal equipment: refers to telecommunications equipment for use by a subscriber, which is or is intended to be connected from the subscriber s premises to the public telecommunications network by means of an interface intended for this purpose

Two-way network: refers to a network which allows the sending and receiving of signals (as opposed to a one-way network).

Upload: refers to the transfer of information from a computer to the network, such as sending an e-mail.

Upstream Path: refers to a broad-band (5-65MHz), Many-to-One HFC network segment, which carries RF signals back from all the subscribers homes UP to the network HeadEnd. Together with the downstream path, the Upstream creates BI-Directional network, which enables the deployment of advanced, Two-Way services (such as Fast-Internet-Access, Interactive TV and cable telephony).

VOD: refers to video on demand, a service that allows television viewers to instantaneously select and view video materials (such as movies, television series) at any time they choose (regardless of the broadcast line-up of the channel/s). VOD services also allow the viewer to stop, pause, fast-forward, rewind and restart the viewing, in a similar manner to the operation of a video tape recorder. Due to its highly demanding bandwidth requirements, VOD services are limited for implementation on broadband platforms only.

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The Company hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

MATAV CABLE SYSTEMS MEDIA LTD.

/s/ Shalom Bronstein

Name: Shalom Bronstein

Title:	Chief Financial Officer
Date:	June 30, 2003

/s/ Amit Levin

Name:	Amit Levin
Title:	Chief Executive Officer
Date:	June 30, 2003

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CERTIFICATIONS

I, Amit Levin, certify that:

1. I have reviewed this annual report on Form 20-F of Matav-Cable Systems Media Ltd.;

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4. The registrant s other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

a. designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

b. evaluated the effectiveness of the registrant s disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the Evaluation Date); and

c. presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant s other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant s auditors and the audit committee of registrant s board of directors (or persons performing the equivalent function):

a. all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant s ability to record, process, summarize and report financial data and have identified for the registrant s auditors any material weaknesses in internal controls; and

b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant s internal controls; and

6. The registrant s other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: June 30, 2003

/s/ Amit Levin

Amit Levin
Chief Executive Officer
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I, Shalom Bronstein, certify that:

1. I have reviewed this annual report on Form 20-F of Matav-Cable Systems Media Ltd.;

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4. The registrant s other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

a. designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

b. evaluated the effectiveness of the registrant s disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the Evaluation Date); and

c. presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant s other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant s auditors and the audit committee of registrant s board of directors (or persons performing the equivalent function):

a. all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant s ability to record, process, summarize and report financial data and have identified for the registrant s auditors any material weaknesses in internal controls; and

b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant s internal controls; and

6. The registrant s other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: June 30, 2003

/s/ Shalom Bronstein

Shalom Bronstein
Chief Financial Officer
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MATAV - CABLE SYSTEMS MEDIA LTD

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2002

INDEX

ERNST & YOUNG

Kost Forer & Gabbay
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REPORT OF INDEPENDENT AUDITORS

To the shareholders of

MATAV CABLE SYSTEMS MEDIA LTD.

We have audited the accompanying consolidated balance sheet of Matav Cable Systems Media Ltd. (the Company) and its subsidiaries as of December 31, 2002 and the related consolidated statements of operations, changes in shareholders equity and cash flows for the year ended December 31, 2002. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits. The financial statements for the previous years were audited by other auditors who expressed their unqualified opinion on those financial statements on March 13, 2002.

We did not audit the financial statements of affiliated companies. The Company s share in equity, as reflected in the balance sheet as of December 31, 2002, is adjusted NIS 20,113 thousand, and the Company s share in their profit for the year ended December 31, 2002, is adjusted NIS 11,119 thousand. The financial statements of the affiliated companies were audited by other auditors, whose reports have been furnished to us, and our opinion, insofar as it relates to amounts included for those companies, is based on the reports of the other auditors.

We conducted our audits in accordance with generally accepted auditing standards in the United States and in Israel, including those prescribed by the Auditors Regulations (Auditor s Mode of Performance)-1973. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes 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 management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2002 and the consolidated results of their operations, changes in shareholders equity and cash flows for the year ended December31, 2002, in conformity with generally accepted accounting principles in Israel, which differ in certain respects from those followed in the United States, to the extent summarized in Note 20.

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As explained in note 1b, the financial statements referred to above are presented in values adjusted for the changes in the general purchasing power of the Israeli currency, in accordance with pronouncements of the Institute of Certified Public Accountants in Israel.

Without qualifying our opinion, we draw attention to claims filed against the Company its subsidiaries and affiliated companies as described in Notes 4 and 12.

Tel-Aviv, Israel

/s/ KOST FORER & GABBAY
KOST FORER & GABBAY
A Member of Ernst & Young Global

March 30, 2003
Except for Note 19
for which the date is
June 30, 2003

Kesselman & Kesselman
Certified Public Accountants
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REPORT OF INDEPENDENT AUDITORS

To the shareholders of

MATAV CABLE SYSTEMS MEDIA LTD.

We have audited the consolidated balance sheet of Matav - Cable Systems Media Ltd. (the Company) and its subsidiaries as of December 31, 2001 and the related consolidated statements of operations, changes in shareholders equity and cash flows for each of the two years in the period ended December 31, 2001.
These financial statements are the responsibility of the Company s Board of Directors and management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of an associated company, the Company s share in equity in net interest in which, as reflected in the balance sheet as of December 31, 2001, is adjusted NIS 1,079,000 and the Company s share in the losses of which, is adjusted NIS 1,826,000 in 2001 and the Company s share in the profit of which, is adjusted NIS 858,000 in 2000. The financial statements of the associated company were audited by other independent auditors, whose report has been furnished to us, and our opinion, insofar as it relates to amounts included for this company, is based solely on the report of the other independent auditors.

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

In our opinion, based upon our audits and the report of the other independent auditors, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2001 and the consolidated results of their operations, the changes in shareholders equity and cash flows for each of the two years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in Israel.

Accounting principles generally accepted in Israel vary in certain respects from accounting principles generally accepted in the United States. The application of the latter would have affected the determination of net income for the years ended December 31, 2001 and 2000, and the determination of shareholders equity as of December 31, 2001, to the extent summarized in note 20.

As explained in note 1b, the financial statements referred to above are presented in values adjusted for the changes in the general purchasing power of the Israeli currency, in accordance with pronouncements of the Institute of Certified Public Accountants in Israel.

Without qualifying our opinion, we draw attention to claims filed against the Company and one of its subsidiaries, as described in note 12.

/s/ Kesselman & Kesselman

Tel-Aviv, Israel
March 13, 2002

Kesselman & Kesselman
Certified Public Accountants (Isr.)

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CONSOLIDATED BALANCE SHEETS

Adjusted to the NIS of December 2002

		December 31,		**Convenience translation (Note 2c)**
		2001	**2002**	**December 31, 2002**
	Note	**Adjusted NIS**		**U.S. dollars**
		(In thousands)		
ASSETS				
CURRENT ASSETS:	15			
Cash and cash equivalents		503	7,749	1,636
Trade receivables	3a	73,722	70,010	14,779
Affiliated companies - current account		1,001	-	-
Other accounts receivable	3b	16,002	18,178	3,837
Total current assets		91,228	95,937	20,252
INVESTMENTS AND LONG-TERM RECEIVABLES:				
Investments in affiliated companies	4a	21,339	22,828	4,819
Investments in other companies	4b	25,684	16,551	3,494
Long-term loans granted to employees		2,042	623	132
Severance pay fund	9	-	322	68
		49,065	40,324	8,513
FIXED ASSETS:	5			
Cost		1,909,641	2,025,205	427,529
Less - accumulated depreciation		851,606	1,014,244	214,111

		1,058,035	1,010,961	213,418
OTHER ASSETS AND DEFERRED CHARGES	6			
Net of accumulated amortization		8,151	7,054	1,489
		1,206,479	1,154,276	243,672

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

MATAV - CABLE SYSTEMS MEDIA LTD.

CONSOLIDATED BALANCE SHEETS

Adjusted to the NIS of December 2002

		December 31,		Convenience translation (Note 2c)
		2001	2002	December 31, 2002
	Note	Adjusted NIS		U.S. dollars
			(In thousands)	
LIABILITIES AND SHAREHOLDERS EQUITY				
CURRENT LIABILITIES:				
Bank credit	7	537,841	523,950	110,608
Current maturities of debentures	11	34,311	34,375	7,257
Trade payables	8a	112,714	85,663	18,084
Affiliated companies - current account		9,027	2,733	577
Other accounts payable	8b	53,713	86,226	18,203
Total current liabilities		747,606	732,947	154,729
LONG-TERM LIABILITIES:				
Accrued severance pay, net	9	110	-	-
Loans and debentures (net of current maturities):				
Loans from bank and others	10	189,731	144,801	30,568
Debentures	11	135,002	101,363	21,399
Customers deposits for converters, net of accumulated amortization	2i	19,600	25,283	5,335
Total long-term liabilities		344,443	271,447	57,302

COMMITMENTS AND CONTINGENT LIABILITIES AND COLLATERALS	12			
SHAREHOLDERS EQUITY:				
Share capital:	13			
Ordinary shares of NIS 1.00 par value; Authorized - 100,000,000 shares; Issued and outstanding; (December 31, 2002 and 2001 30,203,918 shares)		49,816	49,816	10,516
Additional paid-in capital		409,332	409,000	86,343
Accumulated deficit		(277,247)	(242,776)	(51,252)
		181,901	216,040	45,607
Less - cost of Company s shares held by a subsidiary (December 31, 2002 1,343,497: December 31, 2001 - 1,370,148 shares)		(67,471)	(66,158)	(13,966)
Total shareholders equity		114,430	149,882	31,641
		1,206,479	1,154,276	243,672

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

March 30, 2003		
Date of approval of the financial statements	Shmuel Dankner Chairman of the Board of Directors	Amit Lavin Chief Executive Officer

MATAV - CABLE SYSTEMS MEDIA LTD.

CONSOLIDATED STATEMENTS OF OPERATIONS

Adjusted to the NIS of December 2002

		Year ended December 31,			Convenience translation (Note 2c)
		2000	2001	2002	Year ended December 31, 2002
	Note	Adjusted NIS			U.S. dollars
		(In thousands)			
REVENUES	2h	483,791	478,362	505,009	106,609

OPERATING EXPENSES:					
Depreciation		116,506	145,007	165,093	34,852
Other operating expenses	16a	301,850	348,463	352,044	74,318
Total operating expenses		418,356	493,470	517,137	109,170
Gross profit (loss)		65,435	(15,108)	(12,128)	(2,561)
Selling, marketing, general and administrative expenses:	16b				
Selling and marketing		66,045	59,082	41,420	8,744
General and administrative		62,186	58,143	47,019	9,925
		128,231	117,225	88,439	18,669
Operating loss		(62,796)	(132,333)	(100,567)	(21,230)
Financial expenses, net	16c	(34,984)	(53,083)	(49,008)	(10,346)
Other income, net	16d	1,026	3,111	283,859	59,924
Income (loss) before taxes on income		(96,754)	(182,305)	134,284	28,348
Taxes on income	14	174	(442)	110,932	23,418
Income (loss) from operations of the Company and its subsidiaries		(96,928)	(181,863)	23,352	4,930
Equity in earnings (losses) of affiliated companies, net	4	(131,024)	(80,329)	11,119	2,347
Net income (loss)		(227,952)	(262,192)	34,471	7,277
Earnings (loss) per ordinary share	2m	(7.88)	(9.09)	1.19	0.25
Earnings (loss) per ADS	2m	(15.77)	(18.18)	2.39	0.5
Weighted average number of shares outstanding	2m	28,914	28,834	28,860	28,860
Weighted average number of ADSs outstanding	2m	14,457	14,417	14,430	14,430

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

MATAV - CABLE SYSTEMS MEDIA LTD.

STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

Adjusted to the NIS of December 2002

	Share capital						
	Number of shares	Amount	Additional paid-in capital	Foreign currency translation adjustments of financial statements of an associated company	Retained earnings (accumulated deficit)	Cost of Company s share held by a subsidiary	Total
	In thousands	Adjusted NIS in thousands					
Balance at January 1, 2000	27,578	47,000	286,249	(841)	213,955	-	546,363
Net loss	-	-	-	-	(227,952)	-	(227,952)
Exercise of stock options by employees and exercise of series 1 warrants (Note 13b and c)	1,207	1,309	*) 55,256	-	-	-	56,565
Erosion in value of dividend proposed in 1999	-	-	-	-	(1,058)	-	(1,058)
Foreign currency translation adjustments	-	-	-	841	-	-	841
Balance at December 31, 2000	28,785	48,309	341,505	-	(15,055)	-	374,759
Net loss	-	-	-	-	(262,192)	-	(262,192)
Exercise of stock options by employees and exercise of series 1 warrants (Note 13b and c)	49	53	*) 2,076	-	-	-	2,129
Acquisition and exercise of Company s Series 1 warrants by a subsidiary	1,370	1,454	*) 65,751	-	-	(67,471)	(266)
Balance at December 31, 2001	30,204	49,816	409,332	-	(277,247)	(67,471)	114,430
Net income	-	-	-	-	34,471	-	34,471
Sale of the Company s shares held by a subsidiary	-	-	(332)	-	-	1,313	981
Balance at December 31, 2002	30,204	49,816	409,000	-	(242,776)	(66,158)	149,882

*) Net of issuance costs.

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

MATAV - CABLE SYSTEMS MEDIA LTD.

STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

	Convenience translation (Note 2c)				
	Share capital	Additional paid-in capital	Accumulated deficit	Cost of Company s shares held by a subsidiary	Total
	U.S. dollars in thousands				
Balance at January 1, 2001	10,516	86,412	(58,529)	(14,243)	24,156
Net income	-	-	7,277	-	7,277
Sale of the Company s shares held by a subsidiary	-	(69)	-	277	208
Balance at December 31, 2002	10,516	86,343	(51,252)	(13,966)	31,641

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

MATAV - CABLE SYSTEMS MEDIA LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Adjusted to the NIS of December 2002

	Year ended December 31,			Convenience translation (Note 2c) Year ended December 31, 2002
	2000	2001	2002	
	Adjusted NIS			U.S. dollars
	(In thousands)			
CASH FLOWS FROM OPERATING ACTIVITIES:				
Net income (loss)	(227,952)	(262,192)	34,471	7,277
Adjustments required to reconcile net income (loss) to net cash provided by (used in) operating activities (a)	220,774	281,289	(126,391)	(26,681)
Net cash provided by (used in) operating activities	(7,178)	19,097	(91,920)	(19,404)
CASH FLOWS FROM INVESTING ACTIVITIES:				
Purchase of fixed assets	(375,927)	(258,186)	(78,773)	(16,629)
	(31,326)	(3,585)	-	-

Investment in affiliated companies (shares and capital notes)				
Repayment of long-term loans to affiliated companies	-	-	470	99
Deposit in trust, net	-	-	1,873	395
Investment in other assets	-	(1,086)	(2,980)	(629)
Proceeds from sale of investment in an affiliated company	-	21,046	311,706	65,803
Proceeds from sales of investment in another company	5,236	-	-	-
Proceeds from sale of fixed assets	686	2,050	1,267	267
Net cash provided by (used in) investing activities	(401,331)	(239,761)	233,563	49,306
CASH FLOWS FROM FINANCING ACTIVITIES:				
Exercise of stock options by employees and exercise of series 1 warrants, net of issuance costs	56,565	2,129	-	-
Acquisition and exercise of Company s Series 1 warrants by a subsidiary	-	(266)	-	-
Sale of the Company s shares held by a subsidiary	-	-	981	207
Sale of debentures of the Company by a subsidiary	-	23,713	-	-
Receipt of long-term loans from banks and others	236,430	25,738	6,632	1,400
Repayment of long-term loans to banks and others	(1,659)	(2,180)	(131,904)	(27,845)
Repayment of debentures	(29,183)	(29,046)	(34,280)	(7,237)
Short-term bank credit, net	203,933	199,441	24,174	5,103
Dividend paid	(226,021)	-	-	-
Net cash provided by (used in) financing activities	240,065	219,529	(134,397)	(28,372)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(168,444)	(1,135)	7,246	1,530
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR	170,082	1,638	503	106
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR	1,638	503	7,749	1,636

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

MATAV - CABLE SYSTEMS MEDIA LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Adjusted to the NIS of December 2002

	Year ended December 31,			Convenience translation (Note 2c) Year ended
	2000	**2001**	**2002**	**December 31, 2002**
	Adjusted NIS			**U.S. dollars**
	(In thousands)			
(a) Adjustments required to net reconcile income (loss) to net cash provided by (used in) operating activities:				
Income and expenses not involving cash flows:				
Equity in losses (earnings) of affiliated companies, net	131,024	80,329	(11,119)	(2,347)
Depreciation and amortization	119,787	146,958	168,913	35,658
Deferred income taxes, net	174	1,567	-	-
Accrued severance pay	1,768	(381)	(432)	(91)
Loss (gain) on:				
Changes in percentage of shareholding in an affiliated company (including from sale of shares)	-	(5,242)	(302,376)	(63,833)
Sale and write-off of investment in other companies	(4,394)	-	9,133	1,928
Sale of fixed assets	88	2,756	45	9
Linkage differences on principal of debentures	329	382	705	149
Linkage differences on principal of long-term loans to banks and other, net	833	1,389	(397)	(84)
Erosion of deposit in trust	-	-	(1,873)	(395)