

AMERICAN ISRAELI PAPER MILLS LTD
Form 20-F
June 28, 2005

Commission File No. 1-4212

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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, 2004

AMERICAN ISRAELI PAPER MILLS LTD.

(Exact name of Registrant as specified in its charter and translation of
Registrant's name into English)

Israel

(Jurisdiction of incorporation or organization)

P.O. Box 142, Hadera 38101, Israel

(Address of principal executive offices)

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

| | |
|--|---|
| Title of each class | Name of each exchange on which registered |
| Ordinary Shares, par value NIS .01 per share | American Stock Exchange |

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

None

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

None

(Title of Class)

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:

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3,996,674 Ordinary Shares, par value NIS .01 per share

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 No .

Indicate by check mark which financial statement item the registrant has elected to follow: Item 17 Item 18

PART I

ITEM 1 - IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable to Annual Reports

ITEM 2 - OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable to Annual Reports

ITEM 3 - KEY INFORMATION

A. Selected Financial Data

American Israeli Paper Mills Ltd. ("AIPM" or the "Company") prepares its financial statements in accordance with Israeli GAAP. Israeli GAAP and U.S. GAAP vary in certain respects, as described in ITEM 18 below.

The following selected financial data is derived from the audited consolidated financial statements of the Company.

The financial data is presented in New Israeli Shekel (NIS) as follows: AIPM made a transition to reporting in nominal New Israeli Shekels (NIS) in 2004, pursuant to the directives of Standard 12 of the Financial Accounting Standards Board in Israel. In the past AIPM's reports were in NIS, adjusted to changes in the exchange rate of the U.S. dollar against the NIS.

The comparison figures for the years 2000 - 2003 are the dollar figures, as reported in the past, multiplied by the exchange rate of the U.S. dollar as at December 31, 2003, the day of the transition to NIS-based reporting pursuant to Standard 12 (\$1 = NIS 4.379). See also note 1b to the financial statements.

Five Fiscal Year Financial Summary

According to Israeli GAAP

(In Thousands of NIS Except Per Share Amounts)

Year Ended December 31

| | 2004 | 2003 | 2002 |
|------------------------|------|------|------|
| Income Statement data: | | | |

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| | | | | |
|---|------------|-----------|-----------|----|
| Net Sales | 482,854 | 465,092 | 455,775 | |
| Operating Income | 53,930 | 46,584 | 36,455 | |
| Share in profits of associated companies, net | 25,072 | 35,549 | 16,727 | |
| Net Income | (2) 62,732 | 60,047 | 37,460 | |
| Selected balance sheet data: | | | | |
| Total Assets | 1,162,387 | 1,253,274 | 1,052,123 | 1, |
| Property, Plant & Equipment (net) | 324,406 | 325,641 | 325,837 | |
| Long-term Debt | 261,269 | 268,052 | 70,257 | |
| Shareholders' Equity | 575,313 | 614,230 | 650,950 | |
| Per Share Data: | | | | |
| Shares Outstanding at End of Year | 3,996,674 | 3,968,295 | 3,918,710 | 3, |
| Net Income per NIS 1 Par value: | | | | |
| Primary | 1,544 | 1,494 | 947 | |
| Fully Diluted | 1,544 | 1,494 | 947 | |
| Dividend per share | (3) 25.12 | (3) 25.12 | (3) 5.30 | |

(1) The consolidated financial statements since 2000 were influenced significantly by the following transactions:

(a) The finalization of the joint venture with Neusiedler AG (NAG), an Austrian corporation, under which a company named Neusiedler Hadera Paper (NHP), was formed, effective January 1, 2000 (by purchasing AIPM's operations in printing and writing paper), and in which NAG holds 50.1% and AIPM holds 49.9% of the shares. Consequently, as of that date, the results of NHP's operations are no longer consolidated with the results of the Company. Since January 1, 2000, AIPM's share in NHP's results is included in the Company's statement of income under the item "Company's share in profits of associated companies." In the balance sheets, AIPM's share in the shareholders' equity of NHP is included in "Investments in associated companies". NHP was renamed in November 2004 and it is now called Mondi Business Paper Hadera Ltd. ("Mondi Hadera").

(b) On March 31, 2000, Kimberly-Clark Corporation (KC) exercised the option that was granted to it in January 2000 and acquired from AIPM 0.2% of the shares in Hogla-Kimberly Ltd. (hereinafter H-K) in return for \$5 million, thereby increasing its holdings in H-K to 50.1%. Consequently, as of the second quarter of 2000, the results of H-K are no longer consolidated with AIPM's consolidated results and AIPM's share in the results of operations of H-K (49.9%) is included in the item "Company's share in the profits of associated companies." AIPM's share in the shareholders' equity of H-K is included in the balance sheets under "Investments in associated companies."

(2) The net income includes a material non-reoccurring gain in the year 2000, (in the sum of NIS 20,086 thousands, originated from the changes in holdings described above) and in the year 2004 (in the sum of NIS 14,440 thousands, originated from certain tax benefits - see "net profit" on page 21)

(3) Dividend for 2001, in the sum of NIS 5.30 per share (\$1.21 per share) was declared in March 2002 and paid in April 2002.

Dividend for 2002, in the sum of NIS 6.31 per share (\$1.44 per share) was declared in March 2003 and paid in April 2003.

Dividend paid in 2003 includes a special dividend for 2003 in the sum of NIS 18.81 per share (\$4.29 per share). Dividend for 2003 in the sum of NIS 25.12 per share (\$5.54 per share) was declared in August 2004 and paid in September 2004.

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According to U.S. GAAP

(In Thousands of re-measured NIS except per share amounts)

| Income Statement and balance sheet data: | Year ended December 31 | | | |
|---|------------------------|-----------|-----------|-----------|
| | 2004 | 2003 | 2002 | 2001 |
| Sales | 482,854 | 481,491 | 492,990 | 451,250 |
| Operating Income | 63,974 | 53,688 | 53,751 | 25,125 |
| Share in profits of associated companies, net | 29,213 | 20,972 | 27,464 | 22,125 |
| Net Income | (1)58,720 | (1)38,469 | 54,624 | 49,125 |
| Total Assets | 1,107,725 | 1,189,215 | 1,026,083 | 966,125 |
| Property, Plant & Equipment (net) | 285,851 | 283,831 | 279,077 | 245,125 |
| Long-term Debt | 261,269 | 268,052 | 76,001 | 80,125 |
| Shareholders' Equity | 520,482 | 550,354 | 602,675 | 569,125 |
| Per Share Data: (re-measured NIS) | | | | |
| Shares Outstanding at End of Year | 3,996,674 | 3,968,295 | 3,918,710 | 3,918,710 |
| Net Income Per Share: | | | | |
| Basic | 14.76 | 9.77 | 13.94 | 12.54 |
| Diluted | 14.52 | 9.69 | 13.81 | 12.41 |
| Dividend per share | (2)25.12 | (2)25.55 | (2)5.77 | (2)5.77 |

For further information about the effect of application of U.S. GAAP, see Item 18.

Exchange Rates

The exchange rate between the NIS and U.S. dollar published by the Bank of Israel was NIS 4.416 to the dollar on May 31, 2005. The high and low exchange rates between the NIS and the U.S.

* See page 3 (footnote 1) explanation of changes in the consolidated statements, resulting in the de-consolidation of Mondi Hadera (as of January 1, 2000) and of H-K (as of March 31, 2000) and their becoming associated companies.

(1) The net income includes a material non-reoccurring loss in the year 2003, in the sum of NIS 16,986 thousands, [representing other than temporary impairment of an investment in an associated company (see Item 18-e)]. A material non-reoccurring gain was included in the year 2000, in the sum of NIS 18,500 thousands, originated from the changes in holdings described above.

A material non-reoccurring gain was included in the year 2004, in the sum of NIS 14,440 thousands, originated from certain tax benefits (see "net profit" on page 21).

(2) Dividend for 2001, in the sum of NIS 5.77 per share (\$1.21 per share)

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was declared in March 2002 and paid in April 2002.

Dividend for 2002, in the sum of NIS 6.61 per share (\$1.44 per share) was declared in March 2003 and paid in April 2003.

Dividend paid in 2003 includes a special dividend for 2003 in the sum of NIS 19.04 per share (\$4.29 per share).

Dividend for 2003 in the sum of NIS 25.12 per share (\$5.54 per share) was declared in August 2004 and paid in September 2004.

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dollar during the six months of December 2004 through May 2005, as published by the Bank of Israel, were as follows:

| Month ----- | High ----- | Low --- |
|----------------|-----------------|-----------------|
| | 1 U.S. dollar = | 1 U.S. dollar = |
| December 2004 | 4.374 NIS | 4.308 NIS |
| January 2005 | 4.414 NIS | 4.308 NIS |
| February 2005 | 4.392 NIS | 4.357 NIS |
| March 2005 | 4.379 NIS | 4.299 NIS |
| April 2005 | 4.395 NIS | 4.360 NIS |
| May 2005 | 4.416 NIS | 4.348 NIS |

The average exchange rate between the NIS and U.S. dollar, using the average of the exchange rates on the last day of each month during the period, for each of the five most recent fiscal years was as follows:

| Period ----- | Exchange Rate ----- |
|-------------------------------------|------------------------|
| January 1, 2000 - December 31, 2000 | 4.067 NIS/\$1 |
| January 1, 2001 - December 31, 2001 | 4.219 NIS/\$1 |
| January 1, 2002 - December 31, 2002 | 4.736 NIS/\$1 |
| January 1, 2003 - December 31, 2003 | 4.512 NIS/\$1 |
| January 1, 2004 - December 31, 2004 | 4.483 NIS/\$1 |

Forward Looking Statements

This Annual Report on Form 20-F contains "forward-looking" statements, within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "1934 Act") (collectively, the "Safe Harbor Provisions"). These are statements that are not historical facts and include statements about our beliefs and expectations. These statements contain potential risks and uncertainties and actual results may differ significantly. Forward-looking statements are typically identified by the words "believe", "expect", "intend", "estimate" and similar expressions. Such statements appear in this Annual Report and include statements regarding the intent, belief or current expectation of the Company or its directors or officers. Actual results may differ materially from those projected, expressed or implied in the forward-looking statements as a result of various factors including, without limitation, the factors set forth below under the caption "Risk Factors" (the Company refers to these factors as "Cautionary Statements"). Any forward-looking statements contained in this Annual Report speak only as of the date hereof, and the Company cautions potential investors not to place undue

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reliance on such statements. The Company undertakes no obligation to update or revise any forward-looking statements. All subsequent written or oral forward-looking statements attributable to the company or persons acting on the company's behalf are expressly qualified in their entirety by the Cautionary Statements.

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B. Capitalization and indebtedness

Not applicable.

C. Reason for the offer and use of proceeds

Not applicable.

D. Risk factors

Macro-economic risk factors

A slowdown in the market may result in a reduction of profitability

A slowdown in the global markets as well as in the Israeli market may cause: a decrease in the demand for the Company's and its associated companies' products, an increase in the competition with imported products and a decrease in the profitability of export and that could result in a reduction in the Group's* sales and a decline in its profitability.

Future legal restriction may negatively affect the results of operations

The Company's activities and its subsidiaries and associated companies' activities are imposed by legal restrictions (such as government policy on various subjects, different demands made by the authorities supervising environmental regulations and governmental decisions to raise minimum wages) . These restrictions may affect the results of operations of these companies.

Any future rise in the inflation rate may negatively affect business

Since the Company possesses a significant amount of CPI-linked liabilities, a high inflation rate may cause significant financial expenses. Consequently, the Company makes hedges from time to time to cover the exposure due to the liabilities. A high inflation rate may also affect wage expenses, which, at the long run, tend to be adjusted to the changes in the CPI.

Changes in the foreign exchange rates may cause erosion in profitability

The Company, its subsidiaries and associated companies are exposed to risks due to changes in the foreign exchange rates, either due to importing raw materials and finished products or due to exporting to international markets. Change in the foreign exchange rates of the different currencies compared to the New Israeli Shekel may cause erosion in profitability and cash flow, especially in the associated companies.

Risk Factors relating to the Company

The company faces significant competition in the markets the Company operates in

The Company operates in the packaging paper and office supplies industries, both of which are highly competitive. In the packaging paper industry the Company faces competition from imported paper. In the office

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equipment sector the Company faces competition from many suppliers that operate in the Company's markets. The associated companies are also exposed to competition in all of their operations. This competition may negatively affect the future results.

For further information see pg. 12 - competition.

* The Group - The Company and its subsidiaries and associated companies

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The Company is exposed to increases in the cost of raw materials.

The increase in the activity of the paper machines, which are based on paper waste as a recycled fiber, makes it necessary to increase collection of paper waste and to add more expensive resources. The lack of enforcement of the Israeli recycling laws, which require waste recycling, makes it difficult to find alternative resources at a competitive cost.

There is an exposure in the associated companies resulting from fluctuation of prices of raw material and of the imported products, which arrive to Israel without customs or entry barriers. Exceptional price increase of raw materials and imported products may have an adversary effect on these Companies' profitability.

The Company is dependent on energy prices.

AIPM's activities are highly dependent on the consumption of energy and therefore are influenced by fuel and electricity prices. AIPM's profitability may suffer if there is an exceptional increase in energy prices.

Credit Risks

Most of the Company's and its subsidiaries' sales are made in Israel to a large number of customers. Part of the sales is made without full security of payment. The exposure to credit risks relating to trade receivables is usually limited, due to the relatively large number of our customers. The Company performs ongoing credit evaluations of its customers to determine the required amount of allowance for doubtful accounts. An appropriate allowance for doubtful accounts is included in the financial statements.

The operations in Turkey may suffer as a result of the Turkish economy.

The Company is exposed to various risks related to its activities in Turkey, where H-K operates through its subsidiary, Ovisan. These risks result from economic instability and high inflation rates, which have characterized the Turkish economy during the past years, and may be repeated and adversely affect Ovisan's activities.

For further information, see "Item 11 - Quantitative and Qualitative Disclosure about Market Risk".

ITEM 4 - INFORMATION ON THE COMPANY

A. History and Development of the Company

The Company was incorporated in 1951 under the laws of the State of

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Israel, and, together with its subsidiaries and associated companies (which together with the Company are referred to as the "Group") is Israel's largest manufacturer of paper and paper products.

The Company's principal executive offices are located at 1 Meizer St., Industrial Zone, P.O. Box 142, Hadera, Israel, Tel: (972-4) 634-9349, fax: (972-4) 633-9740.

The organizational structure of the Company and certain subsidiaries was changed as of January 1, 1999. This change was intended to result in an operational separation between various activities, especially in the paper and board divisions, to allow for better business focus, greater operating efficiency and the formulation of business strategies that facilitate the establishment of additional international strategic alliances.

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Within the framework of the organizational changes, different fields of operations were defined and separated, including printing and writing paper and packaging paper. For each of them a separate management team was assigned.

Over the last few years, the Group has created several new joint ventures as follows:

1. In July 1992, the Group purchased 25% of the shares of Carmel Container Systems Ltd. ("Carmel"), a leading Israeli designer, manufacturer and marketer of containers, packaging materials and related products. As of May 31, 2005, the Group held 26.25% of the shares of Carmel. Other major shareholders in this company are Rand Whitney Inc. (35.46%) and Ampal Ltd. (21.75%). Carmel shares were traded in AMEX and are currently in a process of deregistration and delisting.

2. In 1996, KC acquired 49.9% of the shares of Hogla, a wholly-owned subsidiary of the Company and a leading Israeli consumer products company, which was then renamed Hogla-Kimberly Ltd (H-K). H-K is engaged in the production and marketing of household paper products, hygiene products, disposable diapers and complementary kitchen products. The partnership was intended to expand the local production base in Israel, in order to serve both local and regional demand, and to offer H-K access to international markets. In 1999, H-K purchased Ovisan, a Turkish manufacturer and marketer of diapers and paper products. On March 31, 2000, KC increased its holdings in H-K to 50.1%.

3. Effective January 1, 2000, AIPM entered into a joint venture agreement with NAG, pursuant to which NAG acquired 50.1% of AIPM's printing and writing paper operations. The printing and writing paper operation was separated from AIPM upon the completion of this transaction and was sold to NHP, a subsidiary that was established for this purpose. In return for the acquisition of 50.1% of the shares of the new company, NAG paid to NHP \$10 million in cash and lent to NHP \$10 million. NHP was renamed in 2004 and is now called Mondi Business Hadera Paper (Mondi Hadera).

4. Amnir Recycling Industries Ltd. (Amnir) (a wholly owned subsidiary of AIPM), which is engaged in the collection and recycling of paper and plastic waste and in the confidential data destruction, acquired in 1997 and 1998 20% and 10%, respectively, of Cycle-Tec Recycling Technologies Ltd. (Cycle-Tec), a research and development company which develops a process for manufacturing of a high strength / low cost composite material, based on recycled post consumer plastic and paper, treated with special chemical additives,. As of May 31, 2005, Amnir owned 30.18% of Cycle-Tec.

In 2004 Amnir established a new company in Switzerland for data

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destruction through the operation of mobile shredder trucks at customers sites, in which the Group holds 75% together with a partner that holds 25%. Amnir is exploring the feasibility of penetrating this sector of operation in Europe.

5. In July 1998, the Company signed an agreement with a strategic partner, Compagnie Generale d'Entreprises Automobiles (CGEA), for the sale of 51% of the operations of Amnir Industries and Environmental Services Ltd. (Amnir Environment) in the field of solid waste management (waste disposal and management of transfer stations and landfills) for a purchase price of \$7.8 million. CGEA is an international French company, which is part of the Veolia group and one of the world's leading companies in the field of environmental services. The agreement did not apply to Amnir's operations in collecting and recycling paper and plastic.

6. In March 2000, AIPM and CGEA, on the one hand, and Tamam Integrated Recycling Industries Ltd. (T.M.M) and its controlling shareholders, on the other hand, entered into an agreement pursuant to which AIPM and CGEA acquired through a joint company from T.M.M.'s controlling shareholders 62.5% of the share capital of T.M.M., a leading Israeli company in the solid waste management field, for \$15.85 million. Simultaneously therewith, 100% of Amnir Environment's shares were transferred to T.M.M. in return for an allocation of 35.3% of the shares of T.M.M to the shareholders of Amnir Environment. Following such transaction, AIPM and CGEA owned, together, 75.74% of the shares of T.M.M. In August and September 2000, T.M.M. acquired approximately 3% of its own share capital. In December 2001, and in August 2003 AIPM and CGEA acquired additional

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shares of T.M.M.'s share capital through a joint company (Barthelemi Holdings Ltd.), resulting in an increase in the ownership of shares of T.M.M. by AIPM and CGEA to 88.02% as of May 31, 2005. AIPM holds directly and indirectly 41.6% of TMM's shares and CGEA holds 46.4% of TMM's shares.

Capital Expenditures and Divestitures

The following data is derived from the consolidated financial statements

2004:

The investments in fixed assets of the Company totaled about NIS 31.0 million in 2004 (about \$6.9 million). These investments included:

- Investments of approximately NIS 2.2 million (\$0.5 million) in environmental issues.
- An investment of approximately NIS 2.2 million (\$0.5 million) in a machine for the manufacturing of cores based on Cycle-Tec technology.
- Investments totaling NIS 26.6 million (\$5.9 million) in buildings, equipment, transportation and Information Technology.

2003:

The investments in fixed assets of the Company totaled about NIS 29.2 million in 2003 (about \$6.7 million). These investments included:

- Investments of approximately NIS 2.6 million (\$0.6 million) in environmental issues, mainly in the process of purification of waste from water.
- An investment of approximately NIS 2.6 million (\$0.6 million) in the

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expansion of the output of the packaging paper machine.

- Investments totaling NIS 24 million (\$5.5 million) in buildings, equipment, transportation and Information Technology.

2002:

The investments in fixed assets totaled about NIS 46.8 million (about \$10.7 million). These investments included:

- The payment of approximately NIS 26.8 million (\$6.1 million) in connection with the extension of the lease for property from the Tel Aviv Municipality, for an additional period ending during 2059.
- The completion of the investment in the anaerobic installation in Hadera, Israel as part of the Group's environmental operations. The additional investment in 2002 totaled NIS 3.5 million (\$0.8 million).
- Investments totaling NIS 16.6 million (\$3.8 million) in the renovation of manufacturing and transport equipment.

B. Business Overview

I. The Group's Operations and Principal Activities

The Company is engaged through its subsidiaries in the manufacture and sale of packaging paper, in the collection and recycling of paper and plastic waste and in the marketing of office supplies, mainly to the institutional and business sector. The Company also holds interests in associated companies that deal in the manufacture and marketing of printing and writing paper, household paper products, hygiene products, disposable diapers, complementary kitchen products, corrugated board containers and

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packaging for consumer goods and the handling of solid waste.

In order to serve the paper production activities, the Company, through a wholly owned subsidiary, is supplying engineering services, maintenance, steam and energy, water supply, sewage treatment etc. to the different paper machines located in the main site of the Company in Hadera in return for cost sharing.

The Company operates in its main production site in Hadera according to the following standards:

ISO 9001/2000 - quality management

ISO 14001 - environmental regulations

Israeli Standard 18001 - safety

The principal products produced and/or marketed by the Company, its subsidiaries and associated companies are as follows:

- o Grades of Paper and Board

Printing and writing paper, publication papers in reels, coated paper, carbonless paper, cut-size paper for copy laser and inkjet, copy-book paper, paper for continuous forms, paper for envelopes and direct mailing and various grades of packaging paper and board.

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- o Packaging Products

Folding cartons, corrugated containers, consumer packages, solid board containers and pallets.

- o Household Products

Bathroom tissue, kitchen towels, facial tissue, napkins, disposable tablecloths, sanitary towels, panty shields, tampons, disposable baby diapers, training pants, baby wipes, disposable adult diapers, incontinence pads, cups and plates.

- o Industrial, Hospital and Food Service Products

Toilet paper, towel rolls, C-fold towels, napkins, place mats, coasters, bed sheets, wadding, paper toilet seat covers, disposable bed-pans and urinals, sterilizing paper, bathroom tissue and paper towel dispensers, dispensers for liquid hand soaps and room deodorizing dispensers for washrooms and cleaners, detergents and cleaning complimentary products.

- o Other Products

Aluminum food wraps, cling-film wraps, garbage bags, air purifiers for lavatories, oven baking and cooking trays, office supplies, recycled ground and palletized plastics used by the plastic products industry, compost for soil conditioning and fertilizers for agriculture and landscape planting.

Sales and Marketing

The Group's packaging and wrapping paper products are sold mostly to four main customers in Israel, which operate in the corrugated board sector with whom the Group has a long business relations.

The Group's office supplies products are sold to thousands of customers in the Business to Business sector and to institutions such as governmental offices and banks. About 25% of the sales are made through tenders.

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The Group's paper grades products are sold to publishers, big and medium size printers, converters, and wholesalers some of which are part of the Group, as well as other direct customers.

The Group's household products are marketed mainly through retail marketing chains, stores and the institutional market.

The Group's packaging products are sold to a wide range of customers in different sectors (e.g., industry, agriculture, food and beverage industry), including direct marketing to ultimate customers through subcontractors and agents.

The Group's waste disposal services are provided mostly to municipalities through tenders and directly to other customers. The Group also operates landfills and transfer stations for the handling of solid waste.

The Group's main marketing strategy has the following objectives:

- (a) Maintaining its existing dominant share in the Israeli market of paper grades and household products produced by the Group and imported by it, through short delivery time and prompt

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service, while constantly improving the quality of its products.

- (b) Meeting the growing and changing requirements of the market by adding new products and improving the quality of existing grades of paper in order to meet the technological changes required by new printing equipment and the needs of the customers.
- (c) Exploring new business opportunities in Israel and abroad and increasing the range of its products and the production capacity.

The following table sets forth the consolidated sales in NIS millions(**) by categories of the consolidated segments of operations:

** AIPM made the transition to reporting in nominal New Israeli Shekels (NIS) in 2004, pursuant to the directives of Standard 12 of the Financial Accounting Standards Board in Israel. In the past AIPM's reports were in NIS, adjusted to changes in the exchange rate of the US dollar against the NIS.

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

| Packaging Paper Manufacturing and recycling (1) | | | Marketing Office Supplies (2) | | | Total | | |
|---|-------|-------|----------------------------------|-------|-------|-------|-------|-------|
| 2004 | 2003 | 2002 | 2004 | 2003 | 2002 | 2004 | 2003 | 2002 |
| 367.4 | 332.1 | 314.6 | 115.5 | 133.0 | 141.1 | 482.9 | 465.1 | 455.8 |

The above mentioned segments include the following activities:

1. Packaging paper manufacturing and recycling - manufacturing and marketing of packaging paper, including collecting and recycling of paper waste. The manufacturing of packaging paper relies mainly on paper waste as raw materials.
2. Marketing office supplies - Marketing of office supplies and paper, mainly to institutions.

Raw Materials

The raw materials required for paper and board production are different wood pulps, secondary fibers (i.e., waste paper) and various chemicals and fillers. Pulp is imported primarily from major suppliers in Scandinavia, the United States, Portugal, Austria, Germany, Brazil and South Africa on a regular basis. The bulk of the pulp tonnage purchased is secured by revolving long-term agreements renewed on a yearly basis. Most of the pulp for the printing and

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writing paper manufactured by Mondi Hadera is purchased by Mondi Business Paper (the Austrian parent company), which purchases pulp for its subsidiaries around the world. This ensures fluent supply and better prices.

The pulp for the household products is being imported by H-K with the assistance of K-C.

About 65% of the fibers required in paper production of the Group (including printing and writing paper and household products) come from waste paper, which in some paper grades, is used in lieu of relatively more expensive pulp. The production of packaging and wrapping paper is based mostly on recycled fibers. Therefore, the main raw material used for the production of packaging and wrapping paper is paper waste most of which is collected from various sources by Amnir, a wholly owned subsidiary of the Company. Approximately 200,000 tons per year of waste paper are collected and handled by Amnir, most of which are used by the Group for the production of paper and some of which is sold to tissue paper manufacturers. Apart from the waste paper collected by Amnir there is a use of residue which is created during the production of packages and purchased from the manufacturers of corrugated board.

The main raw material required for the manufacture of corrugated board is board paper. Carmel purchases paper from two main suppliers one of them is a company within the Group.

Since 1996, the Company has been using precipitated calcium carbonate (PCC), a special pigment used for filling and coating paper in order to improve quality. The PCC is manufactured in a plant constructed and operated by Specialty Minerals Israel Ltd. (SMI), which is a wholly owned subsidiary of Minerals Technologies Inc., a U.S. company. In 2004 an agreement was signed between Mondi Hadera and Omya International AG for the supply of PCC for a period of ten years commencing in April 2006. Omya will construct and operate a PCC plant in Israel. The PCC purchased from Omya will replace the PCC purchased from SMI and is expected to be cost saving.

The cost of paper production is affected by fluctuating raw material prices and the cost of water, energy and fuel oil.

Competition

Most of the Group's products that are sold on the local market are exposed to competition with local and imported products. The imported products arrive in Israel exempt from import tariffs, especially from the EEC, EFTA and the USA. The tariffs on imports of fine paper from other countries are in the range of 0% -12%.

The main competitors of the Group in the different fields of operation are Israeli companies which sell mainly imported products, except for sales of baby diapers and hygienic products in which the Group's main competitor is Proctor & Gamble.

In the market for office supplies that are sold directly to institutions and businesses there are numerous local suppliers, that compete with the Company.

The Group collection and paper recycling operation is exposed to local competition by local companies which operate all over the country.

The competition has influence over the selling prices that the Group can charge. The Group competes with the imported products by emphasizing the advantages of having a local supplier by ensuring the customers uninterrupted supply and service on short notice and excellent quality of products.

C. Organizational Structure

As of May 31, 2005, Clal Industries and Investment Ltd. (Clal) beneficially owned 32.90% of the ordinary shares of the Company and Discount Investment Corporation Ltd. (DIC) beneficially owned 18.59% of the ordinary shares of the Company. Clal and DIC agreed to coordinate and pool their voting power in the Company. To our knowledge, IDB Development Corporation Ltd. owns 67.26% of DIC and 61.93% of Clal. See "Item 7 - Major Shareholders and Related Party Transactions."

Significant subsidiaries and associated companies

| Name of the Company | Ownership and Voting |
|---|----------------------|
| Subsidiaries | |
| Amnir Recycling Industries Ltd. | 100.00% |
| Graffiti Office Supplies & Paper Marketing Ltd. | 100.00% |
| Attar Marketing Office Supplies Ltd. | 100.00% |
| American Israeli Paper Mills Paper Industry (1995) Ltd. | 100.00% |
| Datashred 2003 AG | 75.00% |
| Associated Companies | |
| Hogla-Kimberly Ltd. | 49.90% |
| Ovisan Sihhi Bez Sanai Ve Ticaret A.S. | 49.90% |
| Mondi Business Paper Hadera Ltd. | 49.90% |
| Barthelemi Holdings Ltd. | 33.91% |
| T.M.M. Integrated Recycling Industries Ltd. (direct and indirect) | 41.60% |
| Carmel Containers Systems Ltd. | 26.25% |
| C.D. Packaging Systems Limited (direct and indirect) | 63.20%* |
| Cycle-Tec Recycling Technology Ltd. | 30.18% |

D. Property, Plants and Equipment

The Group's principal executive offices and manufacturing and warehouse facilities are located on approximately 69 acres of land in Hadera, Israel, which is 31 miles south of Haifa, a major seaport, and 28 miles north of Tel Aviv. The Company owns 51 acres, and 18 acres are leased from the Israel Land Administration, an agency of the State of Israel, under several leases. The lease periods terminate during future years from 2008 until 2053. Some of this

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land is rented to associated companies, which operate in Hadera.

The Group's facilities in Hadera are housed in two-story plants and several adjoining buildings. Approximately 1,200,000 square feet are utilized for manufacturing, storage and sales and administrative

* The holding in voting shares is 63.05%

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offices. An additional plant owned by H-K is located in a 10-acre plot in Afula, a city in northern Israel. H-K is leasing from the Israel Land Administration in Nahariya, in northern Israel, approximately 6 acres, which are rented to an associated company. In September 2002, the Company signed an agreement with the Tel Aviv Municipality for the extension of the lease period of a real estate lease for a plant in Tel Aviv, that was shut down at the end of 2002, until the year 2059, in return for the payment of \$6.2 million by the Company. The Company is investigating several options for using the land.

The Group also owns a warehouse containing 50,000 square feet situated on three acres in the Tel Aviv area rented to third party, and a two-acre parcel in the industrial zone of Bnei Brak, near Tel-Aviv, which is used for waste paper collection.

H-K's headquarters and logistic center, which are leased under a long term lease agreement, are located in a new modern site in Zrifin, near Tel-Aviv, covering an area of 430,550 square feet, with 188,370 square feet of buildings.

Associated companies rent plant and office facilities in Migdal Haemek and Caesarea and additional warehouses and waste paper collection sites throughout Israel.

The machinery, equipment and assets of the Company are free of any mortgage, lien, pledge or other charge or security interest.

The Group owns six paper machines that are used in the manufacture of various grades of paper and board. Most of the paper production facilities of the Company and its subsidiaries are located in Hadera where it operates five machines with a combined production capacity of over 320,000 tons per year. The Group owns another machine in Nahariya which produces tissue paper with production capacity of 20,000 tons per year.

The Group also operates converting lines for personal care and household paper products in Hadera and Nahariya.

The Group maintains facilities for collecting, sorting and baling waste paper and board in various locations in Israel and a plant for the recycling of urban waste in Afula. It also has a plant in Afula for the production of disposable baby diapers, incontinence absorbent products and feminine hygiene products, a plant in Migdal Haemek for the production of paperboard consumer packages and a plant in Hadera for recycling plastic waste. The Group also operates a second plant for handling and recycling urban waste in Petah Tikva, near Tel-Aviv, and several landfills.

The Company established in 2000 a new co-generation power plant, based on high-pressure steam available from steam drying employed in paper production, for a total investment of about \$14 million. The operation of the power plant,

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situated in Hadera, and the Group now enjoys an independent power generation capacity of 18MW, with generation costs considerably lower than the cost of electricity purchased from the Israel Electricity Company. As part of this project, the infrastructure of the main electricity supply system was renovated and improved, utilizing modern technological innovations.

The Company is promoting a project for establishing a combined cycle co-generation plant based on natural gas at Hadera. In addition, the Company is preparing for the conversion of its energy-generation systems to natural gas, once the transportation infrastructure of natural gas to Hadera is completed. This conversation is expected to enable savings in production costs, while further improving environmental compliance. The capacity of the plant is expected to enable the Company to sell electricity to external users, including the Israel Electric Company.

In October 2004 a wholly owned subsidiary of the Company, American Israeli Paper Mills Paper Industry (1995) Ltd., was granted by the Minister of National Infrastructure a basic permit to generate electricity by means of power and heat systems (co-generation). In addition, in December 2004 the project was announced as "a National Infrastructure Project".

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Environmental Regulation Matters

The business license of the main production site of the Group in Hadera includes conditions regarding sewage treatment, effluent quality, air quality and the handling of waste and chemicals. In addition, the site has to operate according to the conditions of the Israeli water commission regarding effluent disposal.

Certain of the Group's manufacturing operations are subject to environmental and pollution control laws in Israel. In order to comply with these laws, the Group planned and acquired, during 2001, a new modern facility for the treatment of effluent using an anaerobic treatment process. This process was installed in the Group's site in Hadera as a pre-treatment phase in the existing system based on aerobic treatment, in order to improve the treated effluent quality in compliance with environmental regulations.

In 2003 the Group recorded a significant improvement in sewage waste quality, following the conclusion of the running-in and the optimization of its anaerobic process facility and a significant reduction in sewage quantity.

During the years 2000-2004 the Group invested approximately \$6 million in projects intended to enable it to comply with the strict environmental regulations applicable to it out of which \$1 million was invested during 2004. In addition, at the beginning of 2005 the Group had installed and began operating a sand filter as tertiary treatment for its effluent in the site in Hadera. The investment in this project was approximately \$400,000.

The Company is promoting a project for establishing a combined cycle co-generation plant based on natural gas at Hadera. This project is expected to contribute and improve the environmental compliance since the Company will use natural gas instead of fuel oil.

The Group's achievements in the environmental protection during the last few years were acknowledged at the end of 2002, when the paper mills at the Hadera site won the Shield for Environmental Excellence in Industry Award granted by the Israeli Ministry of the Environment. In 2004 all plants at the main Hadera site passed successfully various environmental inspections.

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ITEM 5 - OPERATING AND FINANCIAL REVIEW AND PROSPECTS

Critical Accounting Policies and Estimates

The Company's discussion and analysis of the financial condition and operations are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in Israel (for information as to the reconciliation between U.S. and Israeli GAAP, see Item 18). The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities.

The Company identified the most critical accounting principles upon which its financial status depends. The Company determined the critical principles by considering accounting policies that involve subjective decisions or assessments.

The Company states its accounting policies in the notes to the consolidated financial statements and at relevant sections in this discussion and analysis.

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This discussion and analysis should be read in conjunction with the Company's consolidated financial statements and related notes included elsewhere in this report.

The Company identified the following to be the most critical accounting policies:

Inventories

The inventory is valued at the lower of cost or market, where cost is determined on the moving average basis. The Company writes down its inventory for estimated obsolescence or unmarketable inventory based on analysis of inventory aging, assumptions about future demand and market conditions. If actual demand and/or market conditions are less favorable than those projected by management, additional inventory write-downs may be required.

Allowance for doubtful accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. The Company provides an allowance for doubtful accounts as a percentage of all specific debts doubtful of collection. The allowances are based on the likelihood of recoverability of accounts receivable considering the aging of the balances, the Company's historical write-off experience, net of recoveries, change in credit worthiness of the customers, and taking into account current collection trends that are expected to continue. These estimated allowances are periodically reviewed, analyzing the customers' payment history. Actual customer collections could differ from the Company's estimates.

Contingencies and risks involving the business

The Company is subject, from time to time, to various claims arising in the ordinary course of operations. In determining whether liabilities should be recorded for pending litigation claims, the Company assesses, based on advice of its outside legal counsel, the allegations made and the likelihood that it will successfully defend itself.

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When the Company believes that it is probable that it will not prevail in a particular matter, it then estimates the amount of the liability. The evaluation of the probability of success of such claims and the determination of whether there is a necessity to include provisions in respect thereof require judgment by the Company's legal counsel and management.

Deferred income taxes

Deferred taxes are determined utilizing the asset and liability method, based on the differences between the amounts presented in the financial statements and those taken into account for tax purposes, in accordance with the related tax laws. Valuation allowances are included in respect of deferred tax assets when it is more likely than not that such assets will not be realized. The Company has considered future taxable income and tax planning strategies in assessing the need for the valuation allowance. Management evaluates the realizability of the deferred tax assets on a current basis. If it were determined that the Company would be able to realize the deferred tax assets in excess of its net recorded amount, an adjustment to deferred tax assets would increase income.

Impairment in value of Long-Lived Assets (including fixed assets and investments in associated companies)

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

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Accordingly, at each balance sheet date, the company assesses whether any events have occurred or changes in circumstances have taken place, which might indicate that there has been an impairment of one or more of the above assets. When such indicators of impairment are present, the Company evaluates whether the carrying value of the asset in the Company's accounts can be recovered from the cash flows anticipated from that asset.

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

Through December 31, 2002, the Company applied the provisions for assessing and recording impairment of assets, prescribed by the U.S. standard, FAS 121.

Discontinuance of Adjusting Financial Statements for Inflation

In October 2001, the IASB issued Israel Accounting Standard No. 12 - "Discontinuance of Adjusting Financial Statements for Inflation" (hereinafter - Standard 12), which provided for the discontinuance of adjusting financial statements for the effects of inflation, as of January 1, 2003. In December 2002, Accounting Standard No. 17 was issued that postponed the date from which Accounting Standard No. 12 is to be applied until January 1, 2004.

The Company's financial statements were drawn up in NIS adjusted for

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the changes in the dollar (as allowed by section 29(b) of Opinion 36 of the Israeli Institute) until December 31, 2003. Based on Standard 12 and the provisions in paragraph 4 to Israeli Accounting Standard No. 13, with effect from January 1, 2004, the Company is no longer able to measure its operations in dollars, and its operations are measured in NIS. The inflation-adjusted NIS amounts as of December 31, 2003, are the base for the nominal-historical financial reporting following January 1, 2004.

See also note 1b to the financial statements.

As for information regarding the effects of new Israeli accounting standards - see note 1q to the financial statements.

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A. Operating Results

The following is a summary of the period-to-period changes in the principal items included in the Consolidated Statements of Income:

Amount and Percentage Increase (Decrease)

| | New Israeli Shekels (in thou) | | |
|--|-------------------------------|---------|----------|
| | Year ended 12/31/04 | | Year e |
| | v. | | year e |
| | year ended 12/31/03 | | year e |
| | ----- | | ----- |
| | Changes | % | Changes |
| | NIS | | NIS |
| | ----- | | ----- |
| Net sales | 17,762 | 3.8 | 9,317 |
| Cost of sales | 13,719 | 3.8 | (1,586) |
| | ----- | | ----- |
| Gross profit | 4,043 | 3.9 | 10,903 |
| Selling, administrative and general expenses | (3,303) | (5.9) | 774 |
| | ----- | | ----- |
| Income from ordinary operations | 7,346 | 15.8 | 10,129 |
| Financial expenses - net | 2,871 | (18.0) | (13,001) |
| Other income | (1,609) | (100.0) | 4,551 |
| | ----- | | ----- |
| Income before taxes on income | 8,608 | 26.7 | 1,679 |
| Taxes on income | 4,554 | (59.1) | 2,086 |
| | ----- | | ----- |
| Income from operation of the Company and the consolidated subsidiaries | 13,167 | 53.7 | 3,765 |
| Share in profits of associated companies | (10,477) | (29.5) | 18,822 |
| | ----- | | ----- |
| Net income | 2,685 | 4.5 | 22,587 |
| | ===== | | ===== |

The statements of income for the years ended December 31, 2004, 2003 and 2002 are presented in New Israeli Shekels as explained in Note 1 to the

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Consolidated Financial Statements (See footnote).

The number of New Israeli Shekels which were exchangeable for 1 U.S. dollar increased (decreased) over the prior year by 7.3% , (-7.6%) and (-1.6%) in 2002, 2003 and 2004, respectively. See Note 1 to the financial statements attached and Item 18 for anticipated effect of adoption of accounting pronouncements that have been issued but are not yet required to be adopted.

2004 Compared to 2003

I. Overview of Results of Operations

1. Consolidated Data

Sales amounted to NIS 482.9 million during 2004, as compared with NIS 465.1 million in 2003.

(1) AIPM made the transition to reporting in nominal New Israeli Shekels (NIS) in 2004, pursuant to the directives of Standard 12 of the Financial Accounting Standards Board in Israel. In the past AIPM's reports were in NIS, adjusted to changes in the exchange rate of the US dollar against the NIS.

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

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Operating profit in 2004 amounted to NIS 53.9 million, as compared with NIS 46.6 million in 2003.

Profit after taxes and before AIPM's share in the earnings of associated companies for 2004, amounted to NIS 37.7 million, as compared with NIS 24.5 million in 2003.

2. Net income

Net income amounted to NIS 62.7 million during 2004, as compared with NIS 60.0 million in 2003.

Net income during 2004 includes non-recurring earnings on account of a NIS 14.4 million tax benefit, originating from the influence of the decrease of the corporate tax rate on the reserve for deferred taxes at AIPM and at its associated companies (from 36% to 30% by 2007), along with a tax benefit on account of the exercise of options by employees.

Net income in 2003 included NIS 2.7 million in non-recurring capital gains and in a tax benefit on account of the exercise of options by employees.

Earnings per share in 2004 amounted to NIS 1,544 per NIS 1 par value (\$3.58 per share), as compared with NIS 1,494 per NIS 1 par value (\$3.41 per share) in 2003. The return on shareholders' equity amounted to 10.2% in 2004, as compared with 9.2% in 2003.

II. The Business Environment

A turnaround took place in the Israeli economy since the beginning of 2004, as the economy rebounded, following a severe recession that lasted several

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years. The recovery was expressed by positive growth rates (approx. 4% in 2004, up from 1.3% in 2003), higher demand and a more optimistic outlook in the markets.

Israel has also experienced a certain calm in the security situation lately, which may positively affect the economy, although this calm is not yet reflected in the results in the financial statements presented herein.

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

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

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

The exchange rate of the NIS compared to the USD was revaluated by 1.6% during 2004, as compared with a 7.6% in 2003.

The inflation rate during 2004 amounted to 1.2%, as compared with a negative inflation rate of -1.9% in 2003.

III. Analysis of Operations and Profitability

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

1. Sales

Consolidated sales amounted to NIS 482.9 million during 2004, as compared with NIS 465.1 million in 2003. The growth in sales is attributed to a quantitative increase in packaging paper and in the sale of paper waste to external entities, coupled with an improvement in the prices of fluting and paper waste and a change in the sales mix. On the other hand, the decrease in Graffiti sales served to offset part of this growth.

2. Cost of Sales

Cost of sales amounted to NIS 375.9 million during 2004, as compared with NIS 362.2 million in 2003.

The gross margin - as a percentage of sales - reached 22.1% during 2004 and is similar to 2003.

AIPM managed to maintain a gross margin similar to 2003, despite the rise in raw material prices (paper waste by 13%), energy prices (4%), and water (5%). This was accomplished through growth in sales, higher sales prices and the continued efficiency process in all sectors of operation.

Labor Wages

Wages and salaries included in the cost of sales and in the selling, general and administrative expenses, amounted to NIS 142.4 million in 2004, as compared with

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NIS 137.0 million in 2003.

However, since the figures in 2003 were reported in accordance with the U.S. dollar and due to the influence of changes in the exchange rate of the U.S. dollar on the reporting of 2003 with the transition to reporting according to Standard 12, the adjusted cost of wages in 2003, as presented above, was NIS 3.7 million lower than the nominal cost at the time that amounted to NIS 140.7 million.

Most of the growth compared to 2003 originated from an increase in wages by an average of 3% that was mostly offset by a reduction in personnel and by differences in other payments - primarily bonuses.

3. Selling, General and Administrative Expenses

Selling, general and administrative expenses (including wages) amounted to NIS 53.0 million - or 11.0% of sales - in 2004, as compared with NIS 56.3 million - or 12.1% of sales - in 2003.

4. Operating Profit

Operating profit amounted to NIS 53.9 million - or 11.2% of sales - in 2004, as compared with NIS 46.6 million - or 10.0% of sales - in 2003.

5. Financial Expenses

Financial expenses amounted to NIS 13.1 million during 2004, as compared with NIS 16.0 million in 2003.

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

The financial expenses in 2003 were influenced by the sharp revaluation of the New Israeli Shekel against the dollar (7.6%), which caused a significant increase in the financial expenses during 2003 when financial reporting was adjusted to the dollar.

In 2004, with the transition to reporting in nominal shekels in accordance with Standard 12, AIPM's financial expenses grew slightly, as a result of the effects of the small revaluation this year (1.6%) on AIPM's surplus dollar assets.

The average increase of NIS 60 million in net financial liabilities - compared to 2003 - resulted in an increase in financial expenses during 2004. This growth was partially offset by the decrease in the average interest rate on short-term credit (5% in 2004 as compared with 7.9% in 2003).

6. Taxes on Income

Taxes on income amounted to NIS 3.2 million in 2004, as compared with NIS 7.7 million in 2003.

Taxes on income from current operations amounted to NIS 13.2 million in 2004, as compared with NIS 8.8 million in 2003.

The principal factors behind the growth in tax expenses in 2004 as compared with in 2003 include the growth in earnings before taxes in 2004, as opposed to the tax benefit that was recorded in 2003 on account of the sharp revaluation (erosion of the reserve), due to reporting adjusted to the changes

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in the exchange rate of the dollar.

In June 2004 a law was passed in Israel, effective retroactively from January 1, 2004, that serves to lower the corporate tax rate (36% prior to the amendment) to 35% in 2004 and gradually down to 30% by 2007.

The effect of this change on AIPM's deferred taxes during 2004 (in the consolidated report) amounted to NIS 5.8 million (primarily due to future tax liabilities which were deferred in respect of timing differences in depreciation, which were calculated at an accelerated pace in the tax reports).

Moreover, a tax benefit of NIS 4.2 million was recorded in 2004, on account of the exercise of options by employees.

In view of the above, the tax expenses during 2004, as reported in the financial statements, amounted to NIS 3.2 million.

7. Profit After Taxes and Prior to AIPM's Share in the Earnings of Associated Companies

Profit after taxes and before AIPM's share in the earnings of associated companies for 2004, amounted to NIS 37.7 million, as compared with NIS 24.5 million in 2003.

8. AIPM's Share in Earnings of Associated Companies

The companies whose earnings are reported under this item (according to AIPM's holdings therein)

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include primarily: Mondi Hadera, Hogla-Kimberly, Carmel and TMM.

AIPM's share in the earnings of associated companies amounted to NIS 25.1 million in 2004 (including NIS 4.4 million as our share in a non-recurring benefit recorded in respect of the change in the corporate tax rate on the deferred earnings of the companies), as compared with NIS 35.5 million in 2003.

The following principal changes were recorded in AIPM's share in the earnings of associated companies (2004 - not including the aforementioned tax benefit), compared to 2003:

- AIPM's share in the net income of Mondi Hadera (49.9%) decreased by NIS 3.0 million. Most of the change in the earnings is associated with a decrease in operating profit between the years, that originated primarily from lower margins in exports to Europe, coupled with increased financial expenses in 2004 as a result of the repayment of shareholder loans over the past two years that led to an increase in Mondi Hadera's debt balance.
- AIPM's share in the net earnings of Hogla-Kimberly Israel (49.9%) increased by approximately NIS 1.2 million, primarily due to the ongoing improvement in operating profit at Hogla-Kimberly Israel, as compared with 2003. This improvement was achieved primarily as a result of better prices and quantitative growth, coupled with the continuing efficiency measures, both in logistics and in production, and particularly as a result of the expanded production of Huggies(R) diapers in Afula. The said increase was offset by lower financial revenues in 2004 as compared with 2003, due to the transition to reporting according to Standard 12 and the effects of revaluation differentials on the NIS compared to the USD, on Hogla's linkage

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balance sheet.

- AIPM's share in the net loss of Ovisan (Hogla's subsidiary in Turkey) (49.9%) amounted to NIS 15.4 million in 2004. Ovisan made considerable efforts to increase its volume of operations in the Turkish market during 2004, while tapping into Unilever's nationwide distribution network, which includes a wide logistic network that covers all of Turkey in a wide national spread, as a necessary condition for the preparations for the continued development of Ovisan and the creation of a platform for introducing the Kimberly-Clark Group's international brands. In this capacity, a significant quantitative increase was recorded in 2004 in the Ovisan sales - both to the domestic market and to exports (up about 40% quantitatively) - accompanied by a significant increase in selling and advertising expenses. The Ovisan loss during 2004 was caused as a result of the said change in the Ovisan distribution and sales network, coupled with escalating competition in the Turkish market due to the arrival of additional competitors into the sector, which resulted in lower prices and a need to adjust the value of inventories to the market prices on the balance sheet date. The difficulties that were created in the assimilation of the new reporting system, which accompanied the change in the distribution system, resulted in delays in receiving the data and in difficulties in providing an immediate response to changing market conditions in reducing the losses, as mentioned above.
- AIPM's share in the net profits of the Carmel Group (26.25%) increased by NIS 3.6 million, due to the continuing improvement in the operating profit. The improvement is attributed to the comprehensive efficiency measures being initiated by Carmel, coupled with the growth in the volume of operations.
- AIPM's share in the TMM earnings (41.6%) increased by NIS 1.3 million. The improvement originates from a significant decrease in TMM's elevated financial expenses during 2004, compared to 2003. Among other factors, this is attributed to a decrease in the interest rate over the two years, coupled with financial revenues from local municipalities

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(with which an agreement was reached) due to considerable arrears in their payments. TMM managed to preserve its operating margin during 2004, despite the considerable increase in transportation costs, due to the significant increase in diesel prices (up by an average of 40% compared to 2003) which was not compensated by selling prices since most of the company's agreements are linked to the consumer price index which rose during 2004 by only 1.2% .

2003 compared to 2002

I. Overview of Results of Operations

1. Consolidated Data

Sales in 2003 totaled NIS 465.1 million, as compared with NIS 455.8 million in 2002.

The operating profit in 2003 amounted to NIS 46.6 million, as compared with NIS 36.5 million in 2002.

The financial expenses in 2003 amounted to NIS 16.0 million, as compared with NIS 3.0 million in 2002. The increased financial expenses are

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primarily attributed to the impact of the revaluation on the net monetary balances (see analysis below - Chapter III, Section 5).

2. Net Income and Earnings Per Share

Net profit in 2003 amounted to NIS 60.0 million, as compared with NIS 37.5 million in 2002.

Net profit in 2003 includes NIS 1.0 million in net capital gains, resulting from the sale of apartments that were owned by the Company and that served Company employees in the past, coupled with a NIS 1.6 million tax benefit, on account of the exercise of employee option warrants. The net profit in 2002 included approximately NIS 0.4 million in non-recurring income, net, from the realization of assets and from taxes on account of preceding years.

The Earnings Per Share in 2003 amounted to NIS 1,494 per NIS 1 par value (\$3.41 per share), as compared with NIS 947 per NIS 1 par value (\$2.16 per share) in 2002.

The return on shareholders' equity amounted to 9.2% in 2003, as compared with 5.9% in 2002.

II. The Business Environment

The severe recession that plague the Israeli economy over several years, as part of the global economic crisis, has been accompanied by security events and terrorist attacks and has resulted in negative growth of the Israeli economy during the said period, along with a considerable rise in unemployment, lower domestic demand (due to the lower purchasing power of the public and due to the significant decrease in incoming tourism), coupled with a significant escalation in competition in all sectors.

The said global economic crisis - especially in Europe - has also affected the paper industry and resulted in a supply surplus and consequently in continuing the importing of low-priced paper into Israel. These imports have led to increased competition, especially in fine paper, accompanied by a decrease in selling prices. As a result of the rise in pulp prices during the same period, the margin between selling prices and pulp prices has decreased as well.

Pulp prices rose by an average of approximately 10% in 2003, as compared with 2002

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Despite the difficult business environment, the Group has managed to maintain its operations at full capacity throughout 2003, while expanding its operations in overseas markets.

Signs of a recovery in the Israeli economy began appearing toward the end of 2003, as reflected by low, albeit positive growth (although no growth was recorded in 2003 in per capita terms), coupled with a certain positive change in the business atmosphere in the economy.

The exchange rate of the NIS compared to the U.S. dollar was revaluated by 7.6% in 2003, as compared with a devaluation of 7.3% in 2002.

Inflation was negative in 2003, at -1.9%, as compared with an inflation rate of 6.5% in 2002.

The negative inflation enabled the Bank of Israel to significantly lower the interest rates, by approximately 3.7% in 2003. This has led to a

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lowering of the Prime rate at the commercial banks in 2003, from 10.4% to 6.7%.

III. Analysis of Operations and Profitability

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

1. Sales

The consolidated sales totaled NIS 465.1 million in 2003, as compared with NIS 455.8 million in 2002.

The 2002 consolidated sales included a sum of NIS 7.9 million of sales derived from the Shafir operation that was discontinued as of September 2002.

The NIS 17.2 million increase in sales - net of Shafir's sales in 2002 - originated primarily from a quantitative increase of approximately 6% in packaging paper.

2. Cost of Sales

The cost of sales amounted to NIS 362.2 million in 2003 -77.9% of sales - as compared with NIS 363.8 million -79.8% of sales - in 2002.

The gross margin as a percentage of sales reached 22.1% in 2003, as compared with 20.2% in 2002.

The improved gross margin in 2003 compared to 2002, was achieved due to the Company's ongoing improvements and increased efficiency. The said efficiency was expressed by the increased output of the machines, by less work hours per ton and a decrease in the consumption of energy per ton produced, coupled with the continued reduction of various manufacturing costs.

The improved gross margin was achieved despite a sharp increase in energy prices, following an average increase of approximately 21% in fuel oil prices compared to 2002 (energy expenses grew by NIS 4.8 million, also on account of the transition to low-sulfur fuel oil, due to the demands of the Ministry of the Environment). Furthermore a 23% increase was recorded in water prices.

Labor Wages

The labor wages recorded in the cost of sales, in the selling expenses and in the general and administrative expenses, totaled NIS 137.0 million in 2003, as compared with NIS 125.5 million in 2002.

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The increase in labor expenses originated primarily from an increase in wages in dollar terms, due to the change in the average exchange rate between the two periods, coupled with the updating of wages, to prevent a decrease in real wages as a result of the rise in the CPI in 2002 (as mentioned above, the CPI rose by 6.5% in 2002).

The said increase in wages was partially offset by the decrease in personnel (as a result of efficiency measures and the shutting down of Shafir).

3. Selling, General and Administrative Expenses

The selling, general and administrative expenses (including wages) amounted to NIS 56.3 million in 2003 (12.1% of sales), as compared with NIS 55.5 million (12.2% of sales) in 2002.

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The increase in selling, general and administrative expenses originated primarily from an increase in NIS-denominated expenses (including wages), in dollar terms (due to the low dollar exchange rate, as compared with 2002).

4. Operating Profit

The operating profit amounted to NIS 46.6 million - 10.0% of sales - in 2003, as compared with NIS 36.5 million - 8% of sales - in 2002.

5. Financial Expenses

The financial expenses totaled NIS 16.0 million in 2003, as compared with NIS 3.0 million in 2002.

The financial statements of 2003 were reported in NIS adjusted to the changes in the exchange rate of the dollar.

The Company possesses a surplus of NIS-denominated financial liabilities over financial assets (consisting primarily of notes and short-term bank credit, denominated in NIS). Consequently, whereas a devaluation serves to lower the financial expenses, a revaluation leads to an increase in the financial expenses.

Elevated financial expenses were recorded by the Company in 2003, originating primarily from the dollar revaluation, whereas in 2002, the devaluation led to lower financial expenses (a difference of 15% between the current year and in 2002).

It should nevertheless be stated that the cash-flow-related financial expenses in 2003 (interest expenses net of revenues) amounted to NIS 8.8 million, similar to the amount paid in 2002.

6. Taxes on Income

The expenditure for taxes on income totaled NIS 7.7 million in 2003, as compared with NIS 9.8 million in 2002.

The principal factor behind the decrease in tax expenses in 2003, as compared with 2002, is the difference between the real-term revaluation in 2003 and the real term devaluation in 2002. This devaluation served to decrease the protection on shareholders' equity (measured for tax purposes according to the changes in the Consumer Price Index) and increased the expenditure on taxes in 2002. A high real-term revaluation was recorded in 2003, that contributed to lowering the tax expenditure. (The report for 2003 was adjusted to the change in the exchange rate of the dollar).

7. Profit After Taxes and Before the Company's Share in the Earnings of Associated Companies

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The profit after taxes and before the Company's share in the earnings of associated companies amounted to NIS 24.5 million in 2003, as compared with NIS 20.7 million in 2002.

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8. Company's Share in Earnings of Associated Companies

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

The Company's share in the earnings of associated companies amounted to NIS 35.5 million in 2003, as compared with NIS 16.7 million in 2002.

The following principal changes were recorded in the Company's share in the earnings of associated companies, compared to the preceding year:

- The Company's share in the net profit of Mondi Hadera grew by NIS 1.2 million as a result of the continuing improvement in operating profitability, that was attained primarily due to efficiency measures and the reorganization of operations and marketing at Mondi Hadera. The improved profitability was impaired by a certain decrease in operating profit in the second half of 2003, as compared with the preceding quarters of 2003 (due to the lower margins and the competition against imports), coupled with the increase in financial expenses, primarily on account of the repayment of some of the loans that were received from the shareholders when Mondi Hadera was founded.
- The Company's share in the net earnings of Hogla-Kimberly grew by NIS 19.0 million, as a result of the improved operating profit at Hogla-Kimberly as compared with 2002. This is primarily attributed to the improved efficiency in logistics following the relocation to the central warehouse in Tzrifin and the gradual transition toward the manufacturing of HUGGIES(R) diapers in Afula. Efficiency measures were also initiated at Ovisan (Hogla's subsidiary in Turkey) and were expressed by a significant improvement in the operating profit. The net profit also grew compared with 2002 on account of financial revenues that were recorded at Hogla-Kimberly and at Ovisan in 2003, due to the effects of the revaluation (in the NIS and in the Turkish lira, as compared with the U.S. dollar).
- The Company's share in the net profit of the Carmel Group grew by NIS 2.5 million due to the transition from an operating loss in the preceding quarters, to an operating profit starting with the third quarter of 2003. This improvement is attributed to the comprehensive efficiency measures that are being initiated by Carmel.
- The Company's share in the net profit of TMM decreased by NIS 2.3 million, as a result of higher financial expenses in 2003, as compared with 2002. This is attributed to an increase in bank credit (as a result of an increase in customer debts primarily local municipalities coupled by strategic investments in the development of TMM that were financed using bank credit) and to the real-term interest in CPI terms, that was higher in 2003 than it was in 2002.

B. Liquidity and capital resources

1. Cash Flows

The cash flows from operating activities amounted to NIS 47.1 million in 2004, as compared with NIS 52.7 million in 2003. (The NIS 52.7 million in cash flows in 2003 includes a NIS 16.4 million dividend received from an associated company. Without the said dividend, the cash flows from operating activities would have amounted to NIS 36.3 million in 2003). The improvement in the cash flows from operating activities during 2004 (excluding the said dividend) originated primarily from a smaller increase in the operating working capital during 2004 compared to 2003, despite the growth in operating volumes in 2004.

2. Financial Liabilities

The Company anticipates that its existing credit lines are sufficient for financing its working capital needs. The Company uses its cash flow from operating activities to finance its investments and for repayment of loans and dividend distributions to its shareholders.

Based on the Company's balance sheet, the Company believes that it is unlikely that there will be any difficulties to obtain credit, whether short term debts or long-term debts, to finance anticipated investments.

At December 21, 2003, the Company issued notes - through tender by private placement - in the amount of NIS 200 million, to institutional investors. These notes carry an interest rate of 5.65% per annum (a margin of 1.45% above government notes with a comparable average maturity at the time). The principal will be repaid in seven equal annual installments between the years 2007-2013 (average maturity of 6 years), with both the principal and the interest being linked to the CPI. The notes are not convertible into the Company's ordinary shares and shall not be registered for trade on a public exchange.

The long-term liabilities (including current maturities) amounted to NIS 267.9 million as at December 31, 2004 as compared with NIS 275.0 million as at December 31, 2003.

The Company uses loans from local financial institutions, mostly banks, to finance its activities. As of December 31, 2004, these loans consisted of the following:

1. Short-term credit from banks - see Note 10d to the financial statements attached.
2. Notes - see Note 4a to the financial statements attached.
3. Other liabilities - see Note 4b to the financial statements attached.

For information regarding financial instruments used for hedging purposes and market risks - see Item 11, "Quantitative and Qualitative Disclosure about Market Risk".

The Group may incur additional tax liabilities in the event of inter-company dividend distributions, derived from "approved enterprises" profits. The said dividend distribution from investee companies is in the amount of up to approximately NIS 85 million (of which the Company's share of the additional tax is NIS 15 million, if this dividend is distributed). No account was taken of the additional tax, since AIPM has the ability and the intention that such earnings are to be reinvested and that no dividend would be declared which would involve additional tax liability to the Group in the foreseeable future.

C. Research and development, patents and licenses, etc.

There are no significant investments in research and development activities.

D. Trend information

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For trend information see "The Business Environment and the Influence of External Factors" above.

E. Off Balance sheet Arrangements

The Company does not have any material off balance sheet managements, as defined in Item 5E of the instructions to Form 20-F.

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F. Contractual Obligations

| In NIS In Millions | Total | Less Than 1 Year | 1-3 Years | 3-5 Years | More than 5 Years |
|----------------------------|-------|---------------------|-----------|-----------|----------------------|
| Long Term Debt Obligations | 306.6 | 19.2 | 112.1 | 112.8 | 62.5 |

The company's material obligations are its notes and loans. See note 4 to the financial statements.

ITEM 6 - DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

The following table sets forth certain information with respect to the directors and executive officers of the Company:

| NAME ----- | DIRECTOR SINCE ----- | AGE --- | POSITION ----- |
|-----------------------|-------------------------|------------|------------------------------------|
| Directors: ----- | | | |
| Ronit Blum | 2005 | 53 | Director |
| Nochi Dankner | 2003 | 51 | Director |
| Michael Dorsman | 1999 | 40 | Director (until - March 6, 2005) |
| Avi Fischer | 2004 | 49 | Director |
| Aviezer (Gezi) Kaplan | 2001 | 57 | Director (until December 20, 2004) |
| Miri Lent-Sharir | 2000 | 49 | Director (until January 25, 2005) |
| Oren Lieder | 2003 | 57 | Director |
| Zvi Livnat | 2003 | 52 | Director |
| Amir Makov | 2005 | 71 | Director |
| Isaac Manor | 2003 | 64 | Director |
| Amos Mar-Haim | 1984 | 67 | Director |
| Leon Recanati | 1988 | 57 | Director (until July 13, 2004) |

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| | | | |
|-------------------|------|----|--|
| Adi Rozenfeld | 2004 | 51 | Director |
| Meir Shannie | 2001 | 60 | Director (until February 23, 2004) |
| Avi Yehezkel | 2003 | 47 | Director |
| Yaacov Yerushalmi | 1998 | 63 | Chairman of the Board since January 2004 the Company from June 1990 until August 2003 |

The business experience of each of the directors is as follows:

Ms. Ronit Blum is Director of Association of Friends, Tel Aviv Sourasky Medical Center, Formerly, a lieutenant colonel in the Israel Defense Forces.

Mr. Nochi Dankner is Chairman and Chief Executive Officer of IDB Holdings Corporation Ltd., Chairman of IDB Development Ltd., Discount Investments Ltd. and of Clal Industries and Investments Ltd. He serves or served as Chairman and Director in public and private companies of Gaden Group, IDB Group and Bank Hapoalim.

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Mr. Michael Dorsman is a businessman, Chairman of the Board and CEO of D.B.P.L. Public Investments Ltd. and Papaya Investments Ltd.

Mr. Avi Fischer is Director and Co-CEO of Clal Industries and Investments Ltd. and Deputy Chairman of IDB Development Ltd, Deputy CEO of IDB Holdings Corporation Ltd., director of Discount Investment Ltd. and several public and private companies of Gaden Group and IDB Group. Senior partner of Fischer, Behar, Chen & Co. Law Office.

Mr. Oren Lieder is Executive Vice President and CFO of Discount Investments Ltd. He serves as a director of various companies, including publicly-traded companies. Formerly served as CFO of Bezeq, the Israeli Telecom Company Ltd.

Mr. Zvi Livnat is Co-CEO of Clal Industries and Investments Ltd. , Deputy CEO of Commerce of Taavura Holding Group Ltd., Deputy CEO of IDB Holdings Corporation, Deputy Chairman of IDB Development Ltd., director in Discount Investments Ltd., and other public and private companies.

Mr. Amir Makov is the Chairman of The Israel Institute of Petroleum & Energy and a director in the following companies: Bank Leumi Le-Israel, ICL Fertilizers (Dead Sea Works, Rotem Amfert Negev), ICL Industry Products (Dead Sea Bromine Company, Dead Sea Periclase), Granite Hacarmel Investments Ltd. and an external director in Wolfman Industries and Ludan Engineering Co. Ltd. Mr. Makov served as an external director of the Company between 1996-2001.

Mr. Isaac Manor is a director of various publicly-traded and privately-held companies within the IDB Group, IDB Holdings Ltd., IDB Development Ltd., Discount Investment Ltd. and Clal Industries and Investments Ltd , Israel Union Bank Ltd. and others and Co-CEO and Chairman of companies in the David Lubinsky Group Ltd.

Mr. Amos Mar-Haim is a member of the Israel Accounting Standards Board and a director of various companies and formerly Vice Chairman of the Israeli Corporation Ltd.

Mr. Adi Rozenfeld is a businessman, consultant to companies and a

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representative of Aactiva Holdings BV in Israel. He is also the Honorary Consul of Slovenia in Israel and a director of various companies.

Mr. Avi Yehezkel is an external director at Bank Yahav. He served as a Knesset member between 1992-2003, during these years, alternately, he served as Deputy Minister of transportation, Chairman of the Economics Committee, Chairman of the Defense Budget Committee, Chairman of the Capital Market Sub-Committee, Chairman of the Banking Sub-Committee and member of the Finance Committee.

Mr. Yaacov Yerushalmi is Chairman of the Board of the Company since January 1999 and Chief Executive Officer of the Company from June 1990 until April 2003.

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Senior Management (as of May 31, 2005)

| Name ---- | Age --- | Position and Business Experience for past five years ----- |
|-----------------|------------|---|
| Avi Brener | 52 | Chief Executive Officer since January 1, 2005 |
| Israel Eldar | 60 | Corporate Controller and responsible for risks and b management. A director of subsidiaries and affiliat Company. |
| Ofra Gorni | 52 | Business Development Manager and a director of subsi affiliated companies of the Company. |
| Lea Katz | 55 | Legal counsel and Corporate Secretary . |
| Gabi Kenan | 61 | Senior Manager |
| Pinhas Rimon | 65 | General manager of Packaging Paper and Recycling Div subsidiaries and affiliated companies of the Company |
| Gideon Liberman | 55 | General Manager of Development and Infrastructure Di |

Senior Management in Subsidiaries and Affiliated Companies (as of May 31, 2005)

| Name ---- | Age --- | Position in the Company ----- |
|---------------|------------|--|
| Arik Schor | 49 | General Manager, Hogla-Kimberly Ltd. |
| Avner Solel | 51 | General Manager, Mondi Business Paper Hadera Ltd. |
| Moshe Riani | 46 | General Manager, Graffiti Office Supplies & Paper Ma |
| Rafi Alon | 58 | General Manager, T.M.M. Integrated Recycling Industr |
| Doron Kempfer | 55 | General Manager, Carmel Container Systems Ltd. |

B. Compensation

The aggregate amount of remuneration paid to all directors and the above senior officers of the Company as a group for services provided by them to the Company during 2004 was approximately NIS 10,175,000 (approximately \$2,362,000). The aggregate amount set aside for pension, retirement or similar benefits for directors and officers as a group for services provided by them to the Company during 2004 was approximately NIS 850,000 (approximately \$197,000).

Out of the above mentioned remuneration, the remuneration paid by the Company in 2004 to Mr. Yerushalmi, the Company's Chairman of the Board, for services provided by him to the Company during 2004, was NIS 2,727,686 (approximately \$633,000).

On May 7, 2001, the Company's Board of Directors adopted an incentive plan, which was subsequently approved by the Company's shareholders, to remunerate the Company's Chairman of the Board of Directors. According to the plan, such remuneration will be equal to the increase in the value of 50,000 ordinary shares of the Company in the period from May 7, 2001 (share price - NIS 194.37 adjusted according to the plan) to May 7, 2008. The remuneration will be spread over the period commencing two years from the resolution of the Board of Directors, until the seventh anniversary of such resolution. As of May 31, 2005 the Chairman of the Board of Directors exercised one quarter of the plan in the sum of NIS 930,000 (approximately \$215,000). A liability was included in the financial statements in respect of the above plan, under current liabilities.

Remuneration of Directors

The remuneration of the directors (including the external directors) for 2004 was approved at the 2004 general meeting of shareholders. Pursuant to regulations under the Israeli Companies Law, each external director of the Company must receive the same annual compensation, which must be between NIS 28,361 and NIS 46,081, plus an additional fee for each meeting attended which must be between NIS 998 and NIS 1,772. The Board approved in 2000 that the remuneration of each director, including the external directors, be fixed at NIS 39,000 plus an additional NIS 1,500 for each meeting attended. The same amounts were approved by the Board in 2001. In 2002, the Board of Directors resolved that the remuneration of each director will be NIS 35,000 plus NIS 1,350 for each meeting attended (a decrease of 10% compared to 2001), subject to the approval of the Company's shareholders. In 2003 and 2004 the Board of Directors resolved that the remuneration of each director will be the same as in the years 2000 and 2001, namely, NIS 39,000 plus an additional NIS 1,500 for each meeting attended. The remuneration was also approved by the General Meeting of Shareholders.

C. Board practices

The directors of the Company, except for the external directors, retire from office at the Annual General Meeting of Shareholders and are eligible for re-appointment at such Annual General Meeting.

Notwithstanding the aforesaid, if no directors were appointed at any Annual General Meeting, the directors appointed at the previous Annual General Meeting shall continue in office. Directors, except for the external directors, may be removed from office earlier by a resolution at an Annual General Meeting of Shareholders.

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The Articles of Association of the Company provide that any director may, by written notice, appoint any person who is approved by the directors to be an alternate director and to act in his place and to vote at any meeting at which he is not personally present. The alternate director is entitled to notice of Board meetings and he will be remunerated out of the remuneration of the director appointing him. The alternate director shall vacate his office if and when the director appointing him vacates his office as director, or removes him from office by written notice.

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There are no services contracts which give the current directors of the Company any benefits upon termination of appointment, except for Mr. Yaacov Yerushalmi, whose terms of employment were submitted for approval at the Annual General Meeting of Shareholders according to Israeli law.

External Directors

Under the Israeli Companies Law, which became effective on February 1, 2000, the Company (as a public company) is required to have at least two external directors as members of its Board of Directors. An external director may not have any financial or other substantial connection with the Company and must be appointed at the Annual General Meeting of Shareholders. The external directors are elected for a three-year term of office that may be extended for another three years. Currently the external directors are Ms. Blum and Mr. Makov.

Audit Committee

Under the Israeli Companies Law, members of the Audit Committee are to be elected from members of the Board of the Company by the Board. The Audit Committee will be comprised of at least three directors, including all of the external directors, but excluding: (i) the chairman of the board of directors; (ii) any director employed by the Company or who provides services to the Company on a regular basis; or (iii) a controlling shareholder of the Company or his relative.

The role of the Audit Committee under the Israeli law is: (i) to examine flaws in the business management of the Company in consultation with its auditors and to suggest appropriate courses of action and (ii) to decide whether to approve actions or transactions which under the Israeli Companies Law require the approval of the Audit Committee (transaction with a related party, etc.) The Company does not have a Nominating Committee nor a Compensation Committee.

The Company's Audit Committee members are: Amos Mar-Haim, Chairman, Ronit Blum, and Amir Makov.

D. Employees

As of April 30, 2005, the Group had 3,197 employees in Israel. The Company and its subsidiaries had 717 employees in Israel of whom 141 were engaged in the office supplies activities, 222 in recycling activities, 138 in packaging paper activities, 153 in infrastructure activities and 63 were management and clerical personnel at the Company's headquarters in Hadera. The associated companies had 2,480 employees in Israel of whom 938 were engaged in the household paper activities, 296 in the printing and writing paper activities, 662 in the recycling activities and 584 in the corrugated board containers activities.

Some of the employees are subject to the terms of employment of

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collective bargaining agreements. The parties to such collective bargaining agreement are the Company and the employees, through the union.

E. Share ownership

In January 1998, the Company's Board of Directors approved a stock option plan, pursuant to which options for ordinary shares were allocated to senior officers of the Company and its subsidiaries, including 32,000 options to the CEO, in three annual installments. The plan was approved at the Company's Annual General Meeting of Shareholders in February 1998 and expired in 2003

In April 2001, the Board of Directors of the Company adopted a new stock option plan under which options to purchase a total of 194,300 shares may be granted to senior officers of the Company and certain other companies in the Group. All of the options were granted in July 2001. Each option is exercisable to purchase one ordinary share of NIS 0.01 par value of the Company. The options vest in

four yearly installments. The vesting period of the first installment is two years, commencing on the date of grant, and the next three installments vest on the third, fourth and fifth anniversary of the grant date. Each installment is exercisable for two years from the vesting date of such installment. For further information regarding the 2001 plan, see Note 6 of the Notes to the Consolidated Financial Statements.

In 2004, 55,525 options were exercised under the 2001 plan and 24,295 shares were issued following the exercise of options.

In August 2001, the Company's Board of Directors approved a stock option plan for employees of the Company and its subsidiaries. Under this plan, up to 125,000 options may be granted without consideration. Each option is exercisable to purchase one ordinary share of NIS 0.01 par value of the Company. In November 2001, 81,455 options were granted under the 2001 employee plan. For further information regarding the 2001 employee plan, see Note 6 of the Notes to the Consolidated Financial Statements.

In 2004 8,615 options were exercised under the 2001 employee plan and 4,084 shares were issued following the exercise of options.

ITEM 7 - MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

A. Major shareholders

The following table sets forth, as of May 23, 2005, the number of Ordinary Shares of the Company beneficially owned by (i) all those persons who, to the Company's knowledge, were the beneficial owners of more than 5% of such outstanding shares, and (ii) all officers and directors of the Company as a group:

| Name and Address: | Amount Beneficially Owned |
|-------------------------|---------------------------|
| Principal Shareholders: | Directly or Indirectly* |
| ----- | ----- |

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| | |
|--|---------------|
| Clal Industries Ltd. ("Clal") 3 Azrieli Center, the Triangle Tower, Tel Aviv, Israel | 1,315,709 (1) |
| Discount Investment Corporation Ltd. ("DIC") 3 Azrieli Center, the Triangle Tower, Tel Aviv, Israel | 743,525 (1) |
| Bank Leumi Le Israel Ltd. P.O.B 2, Tel Aviv, Israel (through trust and provident funds) | 248,142 |
| Bank Hapoalim Ltd. 62 Yehuda Halevi St. Tel Aviv, Israel (through trust and provident funds) | 206,967 |
| All officers and directors as a group | ** |

* Beneficial ownership is based on shared voting and dispositive power over the securities listed in the table.

** The officers and directors of the Company own, in the aggregate, less than 1% of the Company's outstanding ordinary shares, except for Nochi Dankner, Isaac Manor and Zvi Livnat whose ownership is set forth in footnote (1) below.

- (1) IDB Holding Corporation Ltd. ("IDBH") holds 64.3% of the equity of and voting power in IDB Development Corporation Ltd. ("IDBD"), which, in turn, holds 67.26% of the equity of and voting power in DIC and 61.93% of the equity of and voting power in Clal. IDBH, IDBD, Clal and DIC are public companies traded on the Tel Aviv Stock Exchange.

Since May 19, 2003 approximately 51.7% of the outstanding share capital of IDBH, is held by a group comprised of: (i) Ganden Investments I.D.B. Ltd. ("Ganden"), a private Israeli company controlled by Nochi Dankner and his sister, Shelly Bergman, which holds 31.02% of the equity of and voting power in IDBH; (ii) Manor Investments-IDB Ltd. ("Manor"), a private Israeli company controlled by Ruth Manor which holds 10.34% of the equity of and voting power in IDBH; and (iii) Avraham Livnat Investments (2002) Ltd. ("Livnat"), a private Israeli company controlled by Avraham Livnat which holds 10.34% of the equity of and voting power in IDBH. Ganden, Manor and Livnat, owning in the aggregate approximately 51.7% of the equity of and voting power in IDBH, entered into a Shareholders Agreement relating, among other things, to their joint control of IDBH, the term of which is until May 19, 2023.

In addition: (a) Ganden Holdings Ltd., the parent company of Ganden, holds approximately 6.44% of the equity and voting power in IDBH; (b) Manor Holdings B.A. Ltd., the parent company of Manor, holds approximately 0.03% of the equity and voting power in IDBH; (c) Avraham Livnat Ltd., the parent company of Livnat, holds approximately 0.04% of the equity and voting power in IDBH; and (d) Shelly Bergman owns, through a private company wholly owned by her, approximately 7.23% of the equity and voting power of IDBH.

Nochi Dankner is Chairman and CEO of IDBH and chairman of IDBD, Clal and DIC., Isaac Manor (the husband of Ruth Manor), and Zvi Livnat (the son of Avraham Livnat) are directors of each of IDBH, IDBD, Clal and DIC.

In 1980 DIC and Clal agreed for a period of ten years (subject to renewal for additional ten year periods) to coordinate and pool their voting power in the Company in order to appoint an equal number of each party's

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nominees to the Board of Directors of the Company, and in order to elect their designees to the Board's Committees. They also agreed to vote en bloc in General Meetings of the Company on the subject of dividend distributions. This agreement has been extended to the year 2010.

The Company estimates that as of April 30, 2005, 9.15% of its outstanding ordinary shares were held in the United States by 1,015 record holders.

All ordinary shares of the Company have equal voting rights.

B. Related Party Transactions

The information is included in the Company's attached Consolidated Financial Statements: For loans to associated companies see Note 2 to the attached financial statements. For a capital note to an associated company, see Note 4b to the attached financial statements. For transactions and balances with related parties see Note 13 to the attached financial statements.

For further information see also Note 9f and 9g to the financial statements attached.

C. Interests of Experts and Counsel

Not applicable to annual reports.

ITEM 8 - FINANCIAL INFORMATION

A. Consolidated Statements and Other Financial Information

See the financial statements included in Item 18.

B. Significant Changes

None.

ITEM 9 - THE OFFER AND LISTING

A. Offer and Listing Details

The Company's ordinary shares are listed on the American Stock Exchange. The trading symbol for the ordinary shares is AIP. The ordinary shares are also listed on the Tel Aviv Stock Exchange.

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The following table sets forth the high and low sale prices of the Company's ordinary shares on the American Stock Exchange and the Tel Aviv Stock Exchange for the periods indicated:

Last full five fiscal years

| | American Stock Exchange | | Tel Aviv Stock Exchange | | |
|---------------|-------------------------|-----|-------------------------|-----|------|
| | High | Low | High | Low | High |
| | \$ | | | NIS | \$ |
| Calendar Year | | | | | |

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| | | | | | |
|-------|-------|-------|--------|--------|-------|
| 2004 | 60.73 | 48.75 | 267.10 | 217.60 | 60.33 |
| ----- | ----- | ----- | ----- | ----- | ----- |
| 2003 | 54.66 | 29.22 | 239.00 | 143.60 | 54.58 |
| ----- | ----- | ----- | ----- | ----- | ----- |
| 2002 | 40.50 | 25.18 | 178.00 | 116.10 | 40.10 |
| ----- | ----- | ----- | ----- | ----- | ----- |
| 2001 | 64.25 | 30.00 | 267.50 | 130.30 | 64.80 |
| ----- | ----- | ----- | ----- | ----- | ----- |
| 2000 | 83.5 | 55.50 | 347.00 | 224.90 | 86.10 |
| ----- | ----- | ----- | ----- | ----- | ----- |

Quarters during last two full fiscal years and first quarter of 2004:

| 2005 Quarter Ended | American Stock Exchange | | Tel Aviv Stock Exchange | | |
|--------------------|-------------------------|-------|-------------------------|--------|-------|
| | High | Low | High | Low | High |
| | ----- | ----- | ----- | ----- | ----- |
| | \$ | | NIS | | \$ |
| | ----- | ----- | ----- | ----- | ----- |
| March 31 | 57.98 | 48.25 | 246.90 | 214.80 | 56.96 |
| | ----- | ----- | ----- | ----- | ----- |
| 2004 Quarter Ended | High | Low | High | Low | High |
| | ----- | ----- | ----- | ----- | ----- |
| | \$ | | NIS | | \$ |
| | ----- | ----- | ----- | ----- | ----- |
| March 31 | 60.73 | 53.01 | 267.10 | 234.90 | 60.33 |
| | ----- | ----- | ----- | ----- | ----- |
| June 30 | 57.25 | 51.30 | 257.30 | 235.70 | 56.65 |
| | ----- | ----- | ----- | ----- | ----- |
| September 30 | 56.40 | 48.75 | 255.20 | 224.70 | 56.95 |
| | ----- | ----- | ----- | ----- | ----- |
| December 31 | 59.00 | 49.20 | 256.90 | 217.60 | 59.21 |
| | ----- | ----- | ----- | ----- | ----- |

- (1) Share prices have been translated from New Israeli Shekels (NIS) to U.S. Dollars at the representative rate of exchange, as reported by the Bank of Israel, on the dates when such high or low prices in NIS were recorded.

| 2003 Quarter Ended | American Stock Exchange | | Tel Aviv Stock Exchange | | |
|--------------------|-------------------------|-------|-------------------------|--------|-------|
| | High | Low | High | Low | High |
| | ----- | ----- | ----- | ----- | ----- |
| | \$ | | NIS | | \$ |
| | ----- | ----- | ----- | ----- | ----- |
| March 31 | 35.50 | 29.22 | 165.20 | 143.60 | 35.25 |

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| | ----- | ----- | ----- | ----- | ----- |
|---------------------|-------|-------|--------|--------|-------|
| June 30 | 46.12 | 35.65 | 200.00 | 163.30 | 46.38 |
| September 30 | 47.20 | 41.10 | 205.70 | 178.60 | 46.19 |
| December 31 | 54.66 | 45.00 | 239.00 | 197.50 | 54.58 |
| | ----- | ----- | ----- | ----- | ----- |
| 2002 Quarters Ended | High | Low | High | Low | High |
| | ----- | ----- | ----- | ----- | ----- |
| | \$ | | NIS | | \$ (|
| | ----- | ----- | ----- | ----- | ----- |
| March 31 | 40.50 | 32.00 | 178.00 | 149.30 | 40.10 |
| June 30 | 32.10 | 26.30 | 149.20 | 125.20 | 31.30 |
| September 30 | 28.60 | 25.18 | 133.60 | 116.10 | 28.60 |
| December 31 | 33.30 | 26.50 | 155.20 | 125.30 | 33.50 |
| | ----- | ----- | ----- | ----- | ----- |

Last full six months prior to filing of this report:

| | American Stock Exchange | | Tel Aviv Stock Exchange | | |
|---------------|-------------------------|-------|-------------------------|--------|-------|
| | High | Low | High | Low | High |
| | ----- | ----- | ----- | ----- | ----- |
| | \$ | | NIS | | \$ (1 |
| | ----- | ----- | ----- | ----- | ----- |
| May 2005 | 51.50 | 46.50 | 227.60 | 204.20 | 52.21 |
| April 2005 | 52.00 | 49.63 | 225.80 | 214.90 | 51.46 |
| March 2005 | 57.25 | 48.25 | 246.70 | 214.80 | 56.96 |
| February 2005 | 57.98 | 53.75 | 246.90 | 234.90 | 56.42 |
| January 2005 | 56.50 | 52.50 | 245.00 | 229.50 | 56.14 |
| December 2004 | 59.00 | 54.83 | 256.90 | 238.30 | 59.21 |

(1) Share prices have been translated from New Israeli Shekels (NIS) to U.S. Dollars at the representative rate of exchange, as reported by the Bank of Israel, on the dates when such high or low prices in NIS were recorded.

ITEM 10 - ADDITIONAL INFORMATION

A. Share Capital

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Not applicable to Annual Reports.

B. Memorandum and Articles of Association

The Company was registered under Israeli law on February 10, 1951 and its registration number with the Israeli registrar of companies is 52-001838-3.

On June 20, 2001, the Company's shareholders approved a new version of the Articles of Association ("Articles").

Objects of the Company

As indicated in Article 5 of the Company's Articles, the Company may, at any time, engage in any branch or kind of business in which it is, expressly or by implication, authorized to engage in accordance with the Articles. The Company may also cease to engage in such businesses, whether or not it has commenced to engage in such branch or kind of business.

Director's Personal Interest

The Israeli Companies Law requires that a director and an officer of a company disclose to the company any personal interest that he may have and all related material information, in connection with any existing or proposed transaction by the company. The disclosure is required to be made promptly and in any event no later than the date of meeting of the board of directors in which the transaction is first discussed.

If the transaction is an extraordinary transaction, the procedure of approval is as described below. Under Israeli law, an extraordinary transaction is a transaction other than in the ordinary course of business, otherwise than on market terms or that is likely to have a material impact on the company's profitability, assets or liabilities.

Subject to the restrictions of the Israeli Companies Law, a director is entitled to participate in the deliberations and vote with regard to the approval of transactions in which he has a personal interest. A director is not entitled to participate and vote with regard to the approval of an extraordinary transaction in which he has a personal interest, the approval of indemnity, exemption or insurance of the directors or the approval of the directors' compensation. If a majority of the directors have a personal interest in a certain decision, they may participate and vote but the issue must be approved also by the audit committee and by the shareholders. If the controlling shareholder has a personal interest in an extraordinary transaction, the issue must be approved also by the audit committee and the shareholders.

Any power of the Company which has not been conferred by law or by the Articles to any other body, may be exercised by the Board. The management of the Company is guided by the Board.

The Board shall formulate the policies of the Company and shall supervise the performance of the office and actions of the General Manager, including inter alia examination of the financial position of the Company and determination of the credit framework which the Company may receive. Without derogating from any power vested in the Board in accordance with the Articles, the Board may, from time to time, at its discretion, decide upon the issuance of a series of debentures, including capital notes or undertakings, including debentures, capital notes or undertakings which can be converted into shares, and also the terms thereof, and mortgage of the property of the Company, in whole or in part, at present or in

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future, by floating or fixed charge. Debentures, capital notes, undertakings or other securities, as aforesaid, may be issued either at a discount or at a premium or in any other manner, whether with deferred rights or special rights and/or preferred rights and/or other rights, all the aforesaid as the Board may, at its discretion, determine.

Except for special cases as detailed in the Articles and subject to the provisions of the Israeli Companies Law, the Board may delegate its powers to the General Manager, to an officer of the Company or to any other person or to the Board committees. Delegation of the powers of the Board may be with regard to a specific matter or for a particular period, at the discretion of the Board.

There are no limitation requirements regarding age affecting directors' ability to serve as directors of the Company. The directors need not be shareholders of the Company in order to qualify as directors.

The Shares -Rights and Restrictions

All of the Company's shares are ordinary shares. Every ordinary share in the capital of the Company is of equal rights, for all intents and purposes, to every other ordinary share, including the right to dividends, to bonus shares and to participation in the surplus assets of the Company upon liquidation, proportionately to the par value of each share, without taking into consideration any premium paid in respect thereof, all the aforesaid subject to the provisions of the Articles.

Each of the ordinary shares entitles the holder thereof to participate at and to one vote at Annual General Meetings of the Company. As described in Item 6.C, all directors, except external directors, stand for election each year at the Annual General Meeting.

Subject to the provisions of the Israeli Companies Law, the Board may resolve upon the distribution of a dividend. When deciding on the distribution of a dividend, the Board may decide that the dividend shall be paid, in whole or in part, in cash or by way of the distribution of assets in specie, including securities or bonus shares, or in any other manner at the discretion of the Board.

Dividends on the Company's ordinary shares may be paid only out of retained earnings, as defined in the Israeli Companies Law, as of the end of the most recent fiscal year or profits accrued over a period of two years, whichever is higher.

The Company may, by resolution adopted at an Annual General Meeting by an ordinary majority, decrease the capital of the Company and of any reserve fund from redemption of capital. For the execution of any resolution as aforesaid, the Board may, at its discretion, resolve any issues, which may arise in connection therewith.

In case of winding up of the Company, the liquidator may determine the proper value of the assets available for distribution and determine how the distribution among the shareholders will be carried out.

The liability of the shareholders is limited to the payment of par value of their ordinary shares.

Under the Israeli Companies Law, each and every shareholder has a duty to act in good faith in exercising his rights and fulfilling his obligations toward the Company and other shareholders and to refrain from abusing his power in the Company, such as in voting at the General Meeting of shareholders on the

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following matters: any amendment to the Articles; an increase of authorized share capital; a merger; or an approval of certain actions and transactions which require shareholder approval.

In addition, each and every shareholder has the general duty to refrain from depriving other shareholders of their rights.

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Furthermore, 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, has the power to appoint or to prevent the appointment of an officer in the Company or any other power toward the Company is under a duty to act in fairness toward the Company. The Israeli Companies Law does not describe the substance of this duty of fairness. These various shareholder duties may restrict the ability of a shareholder to act in what the shareholder perceives to be its own best interests.

Modification of Rights of Shares

If the share capital is divided into different classes, the Company may by resolution adopted at a General Meeting by a special majority (except if the terms of the issuance of the shares of such class otherwise provide) annul, convert, expand, supplement, restrict, amend or otherwise modify the rights of a class of shares of the Company, provided that the consent, in writing, of all the shareholders of such class thereto shall be received or that the resolution shall have been approved by a General Meeting of the shareholders of such class by special majority, or in the event that it was otherwise provided in the terms of the issuance of a particular class of the shares of the Company, as may have been provided in the terms of issuance of such class, provided that the quorum at the class meeting shall be the presence, in person or by proxy, at the opening of the meeting of at least two shareholders who own at least twenty five percent (25%) of the number of the issued shares of such class.

The rights conferred upon the shareholders or owners of a class of shares, whether issued with ordinary rights or with preference rights or with other special rights, shall not be deemed to have been converted, restricted, prejudiced or altered in any other manner by the creation or issuance of additional shares of any class, whether of the same degree or in a degree different or preferable to them, nor shall they be deemed to have been converted, restricted, prejudiced or altered in any other manner by a change of the rights linked to any other class of shares, all the aforesaid unless otherwise expressly provided in the terms of the issuance of such shares.

Shareholders Meeting

The Company shall hold an Annual General Meeting each year not later than fifteen months after the previous Annual Meeting, at such time and place as may be determined by the Board. Any other General Meeting is referred to as a "Special Meeting".

A notice of a General Meeting shall be published in at least two widely distributed daily newspapers published in Hebrew. The notice shall be published at least fourteen days prior to the convocation of the meeting. In addition the Company provides a notice of the meeting and related proxy statement in English to the holders of its Ordinary Shares listed on the records of the Company's registrar and stock transfer agent in the United States.

Apart from the notices as to the General Meeting as above, according to its articles and the Israeli Companies Law the Company is not required to give

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any notice as to the General Meeting, either to the registered shareholders or to shareholders who are not registered, subject to provisions of the Companies Law and/or any other applicable law. The notice as to a General Meeting is required to detail the place, the day and the hour at which the meeting will be held and to include the agenda as well as a summary of the proposed resolutions and any other details required by law.

The board of directors of the Company shall convene a Special Meeting as may be decided by the Board, and shall also convene a special meeting at the demand of any two directors or one quarter of the directors in office or one or more shareholders who hold at least five percent of the issued capital and one percent of the voting rights, or one or more shareholders who hold at least five percent of the voting rights.

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If the Board receives a demand for the convocation of a Special Meeting as aforesaid, the Board shall within twenty one days of receipt of the demand convene the meeting for a date fixed in the notice as to the Special Meeting, provided that the date for convocation shall not be later than thirty five days from the date of publication of the notice, all the aforesaid subject to the provisions of the Companies Law.

In the resolution of the Board to convene a meeting, the Board may, at its discretion and subject to the provisions of the law, fix the manner in which the items on the agenda will be determined and notice given to the shareholders entitled to participate at the meeting.

Each shareholder holding at least 1% of the voting rights is entitled to request the Board to include in the agenda any issue, provided that this issue is suitable to be discussed in a General Meeting.

No business shall be transacted at any General Meeting unless a quorum is present at the time the meeting proceeds to business. A quorum shall be constituted when two shareholders, holding collectively at least twenty five percent of the voting rights, are present in person or by proxy within half an hour from the time appointed for commencement of the meeting, unless otherwise determined in the Articles.

If a quorum is not present within half an hour, the meeting shall stand adjourned for seven days, to the same day of the week at the same time and place, without need for notification to the shareholders, or to such other day, time and place as the Board may by notice to the shareholders appoint.

If a quorum is not present as aforesaid at the adjourned meeting, the meeting shall be canceled.

Voting and Adopting Resolutions at General Meetings

A shareholder who wishes to vote at a General Meeting shall prove to the Company his ownership of his shares. The Board may issue directives and procedures relating to the proof of ownership of shares of the Company.

A shareholder is entitled to vote at a General Meeting or class meeting, in person or by proxy. A voting proxy need not be a shareholder of the Company.

The above shall also apply to any person entitled to shares, provided that at least forty eight hours before the time for the meeting or the adjourned meeting, as the case may be, at which he proposes to vote, he shall satisfy the Board of his right to vote such shares unless the Company shall have previously

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recognized his right to vote the shares at such meeting.

The instrument appointing a proxy (hereinafter "Proxy Appointment") shall be in writing signed by the principal, or if the principal is a corporation the proxy appointment shall be in writing and signed by authorized signatories of the corporation. The Board is entitled to demand that prior to the holding of the meeting, there shall be produced to the Company a confirmation in writing of the authority of signatories to bind the corporation to the satisfaction of the Board. The Board may also issue provisions and procedures relating to such matters.

The Proxy Appointment or an office copy to the satisfaction of the Board shall be deposited at the registered office or at such other place or places, in or outside of Israel, as may from time to time be determined by the Board, either generally or in respect of a specific meeting, at least forty eight hours prior to the commencement of the meeting or the adjourned meeting, as the case may be, at which the proxy proposes to vote on the strength of such Proxy Appointment.

A voting proxy is entitled to participate in the proceedings at the General Meeting and to be elected as chairman of the meeting in the same manner as the appointing shareholder, unless the Proxy Appointment otherwise provides. The Proxy Appointment shall be in form usual in Israel or any other form which may be approved by the Board.

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Each ordinary share entitles the holder thereof to participate at a General Meeting of the Company and to one vote at a poll.

Right of Non-Israeli Shareholders to Vote

There is no limitation on the right of non-resident or foreign owners of any class of the Company's securities to hold or to vote according to the rights vested in such securities.

Change of Control

Under the Articles, the approval of merger as provided in the Israeli Companies Law, is subject to a simple majority at the General Meeting or class meeting, as the case may be, all the aforesaid subject to the applicable provisions of any law. It is also subject to the approval of the boards of the merging companies.

For purposes of shareholders' approval, unless a court rules otherwise, the merger will not be deemed approved if a majority of the shares held by shareholders, other than the shareholders who are also shareholders in the other merging company whose shares are held by the other merging company, or by any person who holds 25% or more of the shares or the right to appoint 25% or more of the directors in the other merging company, vote against the merger. Upon the request of a creditor of either party to the proposed merger, a court may delay or prevent the merger if it 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 any of the parties to the merger. In addition, a merger may not be completed unless at least 70 days have passed from the time that a proposal of the merger has been filed with the Israeli Registrar of Companies.

The Israeli Companies Law also provides that an acquisition of shares of a public company must be made by means of a tender offer if as a result of the acquisition the purchaser would become a 25% shareholder of the company and there is no existing 25% or more shareholder in the company. If there is no

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existing 45% or greater shareholder in the company, the Companies Law provides that an acquisition of shares of 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.

If following any acquisition of shares, the acquirer will hold 90% or more of the company's shares, the acquisition may not be made other than through a tender offer to acquire all of the shares of such class. If more than 95% of the outstanding shares are tendered in the tender offer, all the shares that the acquirer offered to purchase will be sold to it. However, the remaining minority shareholders may seek to alter the consideration by court order.

Under the Israeli Securities Act 1968, any major shareholder who is the beneficial owner of more than 5% of the Company's equity capital or voting securities is required to report this fact and any change in his holding to the Israeli Securities Authority.

C. Material Contracts

- o On August 30, 2004, the Company signed a term sheet for the purchase of natural gas from the partners in the Thetis Sea Group. Pursuant to the term sheet, the Company will purchase natural gas from the Thetis Sea Partnership over a period that will end on the earliest of the following dates:
 1. 15 years.
 2. The date of completion of the delivery of an overall quantity of natural gas as determined in the agreement (minimum 0.4 BCM and maximum 3 BCM assuming that the Company will

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establish a new co-generation plant).

Accordingly, the financial volume of the term sheet ranges from \$35 million to \$260 million over the term of the agreement. This period may be reduced, under certain conditions as set forth in the term sheet. It was further stipulated that the purchase of the natural gas was contingent upon the completion of the laying of a natural gas pipeline to Hadera, by a date to be agreed upon between the parties.

The term sheet is subject to the signing of a binding agreement, which the Company is currently negotiating.

- o In October 2004 a wholly owned subsidiary of the Company, American Israeli Paper Mills Paper Industry (1995) Ltd., was granted by the Minister of National Infrastructure a basic permit to generate electricity by means of power and heat systems (co-generation). In addition, in December 2004 the project was announced as "a National Infrastructure Project".

The basic permit enables the Company to establish a power station generating between 200 to 400 megawatt, in a combined cycle co-generation, based on natural gas at Hadera.

The basic permit is subject to several conditions that have not yet been fulfilled, including compliance with the production license, compliance with the requirements of the electricity law and compliance with specific milestones which are detailed in the permit.

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- o In 2004 the Company granted an undertaking of indemnification to officers and directors of the Company, pursuant to which the Company is undertaking to indemnify them according to the conditions specified in a Letter of Indemnification provided, that the amount of indemnification will not exceed a cumulative amount that is the equivalent of 25% of the Company's equity according to the last (consolidated) financial statements that will be published before the date of the de facto grant of indemnification.

D. Exchange Controls

Foreign Exchange Regulations

There are no Israeli governmental laws, decrees or regulations that restrict or that affect the export or import of capital, including but not limited to, foreign exchange controls on remittance of dividends on the ordinary shares or on the conduct of the Group's operations, except as otherwise set forth in the paragraph below regarding taxation.

E. Taxation

The following information is regarding the Israeli laws only.

Investors are advised to consult their tax advisors with respect to the tax consequences of their purchases, ownership and sales of Ordinary Shares, including the consequences under applicable state and local law and federal estate and gift tax law, and the application of foreign laws or the effect of nonresident status on United States taxation. This tax summary does not address all of the tax consequences to the investors of purchasing, owning or disposing of the Ordinary Shares.

Income Taxes on Dividends Distributed by the Company to Non-Israeli Residents

Subject to the provisions of applicable tax treaties, dividend distributions from regular profits by the Company to a non-resident shareholder are subject to withholding tax of 25%. The portion of dividends paid out of profits earned under an Approved Enterprise tax status of the Company is subject to

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withholding tax at the rate of 15% (in excess of the tax paid by the company when the dividend is paid of these profits - 25% tax).

The same rates generally apply under the Israeli-U.S. Tax Treaty. However, when a U.S. tax resident corporation is the recipient of the dividend, the rate on a dividend out of regular (non-Approved Enterprise) profits may be reduced to 12.5% under the treaty, where the following conditions are met:

- (a) the recipient corporation owns at least 10% of the outstanding voting rights of the Company for all of the period preceding the dividend during the Company's current and prior taxable year; and
- (b) generally not more than 25% of the gross income of the paying corporation for its prior tax year consists of certain interest and dividend income.

Otherwise, the usual rates apply.

United States individual citizens and residents and U.S. corporations generally will be required to include in their gross income the full amount of

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dividends received from the Company with respect to the Ordinary Shares owned by them, including the amount withheld as Israeli income tax. Subject to the limitations and conditions provided in the Internal Revenue Code of 1986, as amended (the "Code"), such persons may be eligible to claim a credit for such withheld amounts against their United States federal income tax liability. As an alternative, the persons enumerated above (provided such persons, in the case of individual taxpayers, itemize their deductions) may elect to deduct such withheld tax from their gross income in determining taxable income (subject to applicable limitations on the deductions claimed by individuals). However, such a credit or deduction may be limited for U.S. alternative minimum tax purposes, depending on the taxpayer's specific circumstances.

Dividend payments on the Ordinary Shares will not be eligible for a dividends received deduction generally allowed to United States corporations under the Code.

Income Taxes and Capital Gains Applicable in Israel and to Non-Israeli Shareholders

The basic tax rate in 2004 applicable to corporations was 35% . Through December 31, 2003, the corporate tax rate was 36%. Pursuant to an amendment to the Israeli Income Tax Ordinance that was enacted in July 2004, the corporate tax rate is to be gradually reduced from 36% to 30%, in the following manner: the tax rate for 2004 will be 35%, in 2005 - 34%, in 2006 - 32%, and in 2007 and thereafter - 30%. The maximum tax rate for individuals is 49%. These rates are subject to the provisions of any applicable bilateral double taxation treaty. Israeli law generally imposes a capital gains tax on the sale of securities and any other capital assets.

Effective January 1, 2003, the capital gains tax rate imposed, on both individuals and corporations upon sale of capital assets and non-traded securities, acquired after that date has been reduced to 25%; capital gains accrued from assets acquired before that date are subject to a blended tax rate based on the relative Periods of time before and after that date that the asset was held.

Effective January 1, 2003, capital gains from the sale of ordinary shares on the Tel Aviv Stock Exchange (or listed on a designated foreign stock market or traded in a foreign stock exchange), accrued by individuals (and certain corporations) whose income in this regard is not classified as business income, derived from January 1, 2003 and thereafter, will in general be liable to capital gains tax of up to 15%. To the extent that the holder of the ordinary shares claims a deduction of financing expenses, the gain will be subject to tax at a rate of 25%.

In addition, if the ordinary shares are traded on the Tel Aviv Stock Exchange (or listed on a designated foreign stock market), gains on the sale of

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ordinary shares held by non-Israeli tax resident investors will generally be exempt from Israeli capital gains tax.

Notwithstanding the foregoing, dealers (both individuals and corporation) in securities in Israel are taxed at regular tax rates applicable to business income.

The U.S. Israeli Tax Treaty exempts U.S. residents who hold an interest of less than 10% an Israeli company, and who held an interest of less than 10% during the 12 months prior to a sale of their shares, from Israeli capital gains tax in connection with such sale. Certain other tax treaties to which Israel is

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a party also grant exemptions from Israeli capital gains taxes.

Tax Reform -subject to the approval of the Israeli Knesset

In May 2005 the Israeli government approved a Reform in the Israeli taxation law, which among other decreases the corporate tax gradually from 35% in 2004 (see above) to 25% in 2010, this law has to be approved also by the Israeli Knesset in order to be valid.

- F. Dividends and Paying Agents
Not applicable to Annual Reports.
- G. Statement by Expert Not applicable to Annual Reports.
- H. Documents on display

A copy of each document (or a translation thereof to the extent not in English) concerning the Company that is referred to in this Annual Report on Form 20-F, is available for public view at our principal executive offices at American Israeli Paper Mills Ltd., 1 Meizer Street Industrial Zone, Hadera 38100, Israel. Copies of this Annual Report and the exhibits hereto may be inspected and copied at the SEC's Public Reference Room at 450 Fifth Street, NW, Washington, D.C. 20549 and at the SEC's regional office at 500 West Madison Street, Suite 1400, Chicago, Illinois 60661. Copies of the materials may be obtained from the Public Reference Room of the SEC at 450 Fifth Street, NW, Washington, D.C. 20549 at prescribed rates. The public may obtain information on the operation of the SEC's Public Reference Room by calling the SEC in the United States at 1-800-SEC-0330.

ITEM 11 - QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

Due to its operations, the Company is exposed to market risks, consisting primarily of changes in interest rates - on both short and long-term loans, changes in exchange rates and changes in raw material and energy prices. These changes affect the Company's results of operations.

The Company's Board of Directors determines the policy according to which financial instruments are employed and defines the objectives to be attained, taking into account the Group's linkage balance sheet and the impact of various changes in currencies and in the Consumer Price Index on the Company's balance sheets and on its financial statements.

AIPM conducts calculations of the its exposure every month and examines the compliance with the policy determined by the Board of Directors.

Furthermore, limited use is made of derivative financial instruments, which the Company employs for hedging the cash flows, originating from the existing assets and liabilities.

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Such transactions are conducted primarily through currency options and forward transactions opposite Israeli banking institutions. The Company therefore believes that the inherent credit risk of these transactions is slight.

As of December 31, 2004 AIPM owns CPI-linked long-term loans (notes) in the total sum of about NIS 235 million. The interest on such loans is not higher than the market interest rate. In the event that the inflation rate shall rise significantly, a loss may be recorded in AIPM's financial statements, due to the

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surplus of CPI-linked liabilities.

In order to hedge this exposure, AIPM has entered into forward transactions, as at December 31, 2004 for hedging NIS 200 million against a rise in the CPI until December 2005. These transactions serve to replace hedging transactions in the same amount that terminated in January 2005.

Credit Risks

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

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

Fair Value of Financial Instruments

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

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

Quantitative Information Regarding Market Risk

The following are the balance-sheet components by linkage bases at December 31, 2004:

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| In NIS Millions | Unlinked | CPI-linked | In foreign currency, or linked thereto (primarily US\$) |
|-------------------------------------|----------|------------|--|
| | ----- | ---- | ---- |
| Assets | | | |
| ----- | | | |
| Cash and cash equivalents | 3.3 | | 4.5 |
| Short-term investments | 16.9 | 45.6 | |
| Other Accounts Receivable | 192.0 | 1.8 | 43.6 |
| Inventories | | | |
| Investments in associated companies | 49.3 | 11.2 | 8.6 |
| Deferred taxes on income | | | |
| Fixed assets, net | | | |

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| | | | |
|---|--------|---------|------|
| Deferred expenses, net of accrued amortization | ----- | ---- | ---- |
| Total Assets | 261.5 | 58.6 | 56.7 |
| | ----- | ---- | ---- |
| Liabilities | | | |
| ----- | | | |
| Credit from Banks | 110.5 | | 2.2 |
| Accounts Payable | 142.8 | 1.0 | 10.1 |
| Deferred taxes on income | | | |
| Notes | | 235.1 | |
| Other liabilities | 32.8 | | |
| Shareholders' equity | | | |
| | ----- | ----- | ---- |
| Total liabilities and equity | 286.1 | 236.1 | 12.3 |
| | ----- | ----- | ---- |
| Surplus financial assets (liabilities) as at December 31, 2004 | (24.6) | (177.5) | 44.4 |

ITEM 12 - DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

Not applicable to Annual Reports

ITEM 13 - DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

None.

ITEM 14 - MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS

None.

ITEM 15 - CONTROLS AND PROCEDURES

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's periodic filings with the SEC is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including the Company's Chief Executive Officer (CEO - the Company's senior executive officer) and Chief Financial Officer (CFO - the Company's senior financial officer), as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can

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provide only reasonable assurance of achieving the desired control objectives. Furthermore, management necessarily was required to use its judgment in evaluating the cost to benefit relationship of possible disclosure controls and procedures. Within 90 days prior to the date of this report, the Company performed an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures. The evaluation was performed with the participation of senior management of each business segment and key corporate functions, and under the supervision of the CEO and CFO. Based on the evaluation, the Company's management, including the CEO and CFO, concluded that the Company's disclosure controls and procedures were effective. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect internal controls after the date the Company completed the evaluation.

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ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT

Amos Mar-Haim a member of the Registrant's Audit Committee, is Audit Committee Financial Experts under the applicable rules and regulations of the SEC. Amos Mar-Haim is "independent", as that term is defined in the American Stock Exchange listing standards.

ITEM 16B. CODE OF ETHICS

The Company has adopted a code of ethics which is applicable to all directors, officers and employees of the Company, including its principal executive, financial and accounting officers and persons performing similar functions (the "Code of Ethics"). The Code of Ethics covers areas of professional and business conduct, and is intended to promote honest and ethical behavior, including fair dealing and the ethical handling of conflicts of interest; support full, fair, accurate, timely and understandable disclosure in reports and documents the Company files with, or submits to, the SEC and other governmental authorities, and in its other public communications; deter wrongdoing; encourage compliance with applicable laws and governmental rules and regulations; and ensure the protection of the Company's legitimate business interests. The Company encourages all of its officers and employees promptly to report any violations of the Code of Ethics, and has provided mechanisms by which they may do so. The Company will provide a copy of the Code of Ethics to any person, without charge, upon written request addressed to the Corporate Secretary of the Company at the Company's corporate headquarters in Hadera, Israel.

ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The Audit Committee maintains a policy of approving and recommending only those services to be performed by the Company's external auditors which are permitted under the Sarbanes-Oxley Act and the applicable rules of the SEC relating to auditor's independence, and which are otherwise consistent with and will encourage, and are remunerated at levels that accord with, the basic principles of auditor independence. The practice of the Audit Committee is to receive from the Company's management, a list of all services, including audit, audit-related, tax and other services, proposed to be provided during the current fiscal year to the Company and its subsidiaries by Kesselman & Kesselman, an affiliate of PricewaterhouseCoopers. After reviewing and considering the services proposed to be provided during the current fiscal year and, where appropriate in order better to understand their nature, discussing them with management, the Audit Committee pre-approves such of the proposed services, with a specific pre-approved budget, as it considers appropriate in accordance with the above principles. Additional services from Kesselman & Kesselman and any increase in budgeted amounts will similarly be pre-approved during the year by the Audit Committee on a case-by-case basis.

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All audit-related and non-audit-related services performed by Kesselman & Kesselman during 2004 were reported to, and the services proposed to be provided by them during 2005 pre-approved by the Audit Committee, in accordance with the procedures outlined above.

The total fees paid by the Company to Kesselman & Kesselman for all services, described above, including audit services, for the years ended December 31, 2004 and 2003 were \$120,000 and \$125,000, respectively.

Item 16D. Exemptions from the Listing Standards for Audit Committees

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Not applicable.

Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers

Neither the Company nor any affiliated purchaser purchased any of the Company's equity securities during 2004.

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PART III

ITEM 18 - FINANCIAL STATEMENTS

The Company prepares its financial statements in accordance with Israeli GAAP. Israeli GAAP and U.S. GAAP vary in certain significant respects, as described below:

a. The functional currency of the Company

Through December 31, 1993, the financial statements of the Company, presented in NIS values adjusted for the changes in the general purchasing power of the Israeli currency based on the changes in the exchange rate of the dollar were also used for the purposes of reporting in conformity with U.S. GAAP applicable to entities operating in hyper-inflationary economic environments, as prescribed by Statement No. 52 of the Financial Accounting Standards Board of the United States (FASB). Since the inflation rate in Israel has decreased considerably, the Company decided that, commencing in 1994, it would implement the rules relating to economies no longer considered hyper-inflationary, for reporting purposes, in accordance with U.S. GAAP.

Under those rules:

- 1) The functional currency of the Company (the currency in which most income is derived and most expenses are incurred) is the New Israeli Shekel (NIS);
- 2) The opening balances for 1994 are the balances presented in the Company's balance sheet at December 31, 1993;
- 3) Transactions performed from January 1, 1994 are presented on the basis of their original amounts in Israeli currency.

The term "Re-measured NIS" signifies the currency used for FASB 52 purposes, as described above.

As to the effect of application of these rules - see (i) below.

As to the discontinuance of the adjustment of the financial statements to the exchange rate of the dollar as from January 2004, see not 1b to the financial statements.

b. Deferred income taxes

Under Israeli GAAP, no deferred taxes are provided for in respect of certain long-lived (more than 20 years) assets, such as buildings and land. Under U.S. GAAP, in accordance with the provisions of FAS 109, income taxes are to be provided for any assets that have a different basis for financial reporting and income tax purposes.

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In addition, for U.S. GAAP purposes deferred taxes are to be provided for with respect to un-remitted earnings of investee companies. Under Israeli GAAP due to the Company's policy to hold its investments in investee companies, and not to realize them, these temporary differences are considered differences permanent in duration for which deferred taxes are not provided for.

Through 1999, as long as the main investments of the Company were subsidiaries which were controlled by the Company, the Company did not provide for deferred taxes also for U.S. GAAP

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reporting purposes, since those differences were deemed to be not taxable due to the tax free inter-company dividend distribution law in Israel and tax planning on its behalf, accordingly.

As from 2000, due to changes in certain of the Company's investments from subsidiaries to associated companies, deferred taxes were provided for any portion that arose from investee companies sources other than pre-1993 undistributed earnings (taking into account the Company's tax strategy).

As to the effect of application of this treatment, see (i) below.

c. Employee stock option plans

Under Israeli GAAP, no compensation expenses are recorded in respect of employee stock options.

Under U.S. GAAP, the Company accounts for employee stock based compensation using the intrinsic value-based model of accounting prescribed by Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees" ("APB 25") and related interpretations. In accordance with FAS 123 - "Accounting for Stock-Based Compensation" ("FAS 123"), the Company discloses pro forma data assuming the Company had accounted for employee stock option grants using the fair value-based method defined in FAS 123.

All of the Company's awards are considered to be variable awards; thus the difference between the price of the shares at each balance sheet date and the exercise price of such options is charged to income over the vesting period and is adjusted in subsequent periods up to the measurement date (exercise or expiration date). The amount of the difference is correspondingly presented as capital surplus.

As to new accounting pronouncement relating to share-based compensation see (l.) bellow.

Pro-forma disclosure

Had compensation cost for the employee stock options plans, been determined based on the fair value at the grant date, consistent with the method of FAS 123, the Company's net income and earnings per share would have been changed to the pro - forma amounts indicated below:

| | Year ended |
|------|------------|
| | ----- |
| 2004 | 2 |
| | ----- |

NIS in thousands, exc

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| | | |
|---|---------|---|
| Net income, as reported under U.S. GAAP | 58,720 | 3 |
| Add (deduct): | | |
| stock based employee compensation expense (income), included in reported net income, net of related tax effect | 8,458 | |
| Deduct: | | |
| stock based employee compensation expense determined under fair value method for all awards, net of related tax effects | (3,523) | (|
| <hr style="border-top: 1px dashed black;"/> | | |
| Pro forma net income -under U.S. GAAP | 63,655 | 4 |
| <hr style="border-top: 1px dashed black;"/> | | |
| Earnings per share - under U.S. GAAP: | | |
| Basic - as reported | 14.76 | |
| Basic - pro forma | 16.00 | 1 |
| Diluted - as reported | 14.52 | |
| Diluted - pro forma | 15.74 | 1 |

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The quoted price of the Company's ordinary shares on December 31, 2004 was NIS 238.3 (\$55.0).

A summary of the status of the Company's plans as of December 31, 2004, 2003 and 2002, and changes during the years ended on those dates, is presented below:

| | 2004 | | 2003 | | 2 |
|---|----------|---|-----------|---|---------|
| | Number | Weighted average exercise Price NIS | Number | Weighted average exercise Price NIS | Number |
| Options outstanding at beginning of year | 216,243 | 159.15 | 333,916 | 147.27 | 333,916 |
| Changes during the year: | | | | | |
| Exercised | (64,140) | 153.82 | (116,175) | 116.37 | |
| Expired | | | (1,498) | 98.62 | |
| <hr style="border-top: 1px dashed black;"/> | | | | | |
| Options outstanding at end of year | 152,103 | 132.74 | 216,243 | 159.15 | 333,916 |
| <hr style="border-top: 1px dashed black;"/> | | | | | |
| Options exercisable at year-end | *54,953 | 99.98 | 70,518 | 179.53 | 58,161 |
| <hr style="border-top: 1px dashed black;"/> | | | | | |

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* Represents the number of options fully vested as of December 31, 2004. Based upon the Company's share market value as of December 31, 2004, this reflects potentially 31,897 shares regarding the options exercisable at year-end.

The fair value of the options granted was computed by the Black-Scholes formula using the following assumptions: dividend yield of 0%; expected volatility of 30.5%; risk-free interest rate (linked to the Israeli CPI) of 4.5% and expected average life 5-5.5 years.

The following table summarizes information about options outstanding at December 31, 2004.

| Options outstanding | | | |
|---|--|--|--|
| Range of Exercise Prices ----- | Number outstanding at December 31, 2004 ---- | Average remaining contractual life ----- Years | Number of op exercisabl December 2004 ---- |
| NIS | | | |
| 68.77 | 30,372 | 1.5 | 30,372 |
| 113.23 | 14,878 | 1.8 | 14,878 |
| 125.18 | 48,575 | 2.5 | |
| 177.37 | 9,703 | 0.5 | 9,703 |
| 177.37 | 48,575 | 3.5 | |
| | 152,103 | 2.4 | 54,953 |
| | ===== | === | ===== |

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d. Earnings per share ("EPS")

Israeli GAAP relating to computation of EPS is described in note 1P to the financial statements attached.

The EPS computation according to U.S. GAAP presented below is in accordance with FAS 128.

As applicable to the Company, the main difference between the two methods of EPS computation is that shares to be issued upon exercise of employee stock options (under SAR plans) are taken into account in the computation of basic EPS in Israel, whereas in the United States, in computing basic EPS, only the weighted average number of company shares actually outstanding in the reported period is taken into account, and shares to be issued upon exercise of options are included in the computation of diluted EPS. Another difference is the U.S. requirement for separate presentation - in the income statements - of basic and diluted EPS as long as they are not identical, while, in Israel, such separate presentation is only required if the difference between basic and diluted EPS is in excess of 5%.

As to the effect of application of U.S. GAAP, see (i) below.

Following are data relating to the weighted average number of shares

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for the purpose of computing basic and diluted earnings per share under U.S. GAAP:

| | 2004 | 2003 | |
|---|-----------|-----------|-------|
| | ----- | ----- | ----- |
| Weighted average number of shares used in the computation of basic earnings per share | 3,978,339 | 3,938,035 | 3,91 |
| Net additional shares from the assumed exercise of employee stock options | 65,375 | 31,673 | 1 |
| | ----- | ----- | ----- |
| Weighted average number of shares used in the computation of diluted earnings per share | 4,043,714 | 3,969,708 | 3,93 |
| | ===== | ===== | ===== |

- e. Investment in marketable equity securities accounted for by the equity method (associated company) - Carmel Container Systems (Carmel)

Under Israeli GAAP, an investment in an associated company is tested for impairment under the provisions of Israeli Standard No. 15 of the Israeli Accountant Standard Board - "Impairment of Assets" (see note 1h to the financial statements). Based on the provisions of this Standard, and as explained in note 2e to the financial statements, the Company determined that the recoverable value of the investment in Carmel exceeds its carrying value (based, among other, on its Discounted Cash Flows), and accordingly, the investment was not written down.

Under U.S. GAAP (APB 18 - "The Equity Method of Accounting for Investments in Common Stock") and SEC Staff Accounting Bulletin (SAB) No. 59 ("Accounting for Noncurrent Marketable Equity Securities"), a decline in value of investment in an associated company which is other than temporary was recognized as a realized loss in 2003, establishing a new carrying value for the investment. Factors considered in determining that a decline is other than temporary included, among other, the length of time and the extent to which the market value has been less than the carrying value of the investment. The relevant market value for determining the impairment loss is the market value at December 31, 2003.

Therefore, although according to the Israeli GAAP the recoverable value of this investment exceeds

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its carrying value (see above) under U.S. GAAP and SEC rules described above, the decline in the market value of Carmel shares was the significant factor in determining other than temporary decline. Accordingly, for U.S. GAAP reporting, since the decline in the market value of Carmel was long and extensive, the Company reduced the carrying value of this investment to its market value as of December 31, 2003 and recorded an impairment loss amounting NIS 16,986,000 (see also share in profits of associated companies under U.S. GAAP in Item 3 above).

Under US GAAP- Since there is no goodwill or non amortizable assets, the impairment is attributed only to Carmel's fixed assets; therefore the Company amortizes the impairment at the rates applicable to Carmel's fixed assets. The amortization of the impairment, as above, resulted in an increase in the share in profits of the associated company amounting to NIS 1,699 thousands

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in 2004.

f. Statements of income presentation

Under Israeli GAAP, the Company included, in the statements of income for the years ended December 31, 2002 and 2003, under "other income (expenses)", in 2002 - loss from closure of facilities and disposal of assets and closing inventories and in 2003 - gain from sale of apartments.

Under U.S. GAAP, the loss from inventories should be classified as part of cost of sales and loss from closure of facilities, disposal of assets and sale of apartments should be classified as part of operating income.

These adjustments were included in the reconciliation to the U.S. GAAP (see operating income under U.S. GAAP in Item 3 above).

g. Accounting for guarantees

The Group's applies for U.S. GAAP purposes the provisions of FASB interpretation No. 45 "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others " ("FIN 45").

FIN 45 applies to guarantees either granted or amended after December 31, 2002. Applying FIN 45 has not had a material effect on the Company.

h. Supplemental disclosure on employee rights upon retirement

The Company and its subsidiaries expects to contribute in 2005 NIS 8,400 thousands to the provident funds and to the insurance companies in respect of its severance pay obligations.

i. The effect of applying U.S. GAAP on the consolidated financial statements is as follows:

1) Consolidated statement of income figures:

| | Year ended ----- 2004 ----- NIS i (except pe |
|--|---|
| Net income, as reported according to Israeli GAAP | 62,732 |
| Effect of treatment of the following items in accordance with U.S. GAAP: | |
| Functional currency* | 4,827 |
| Deferred income taxes - net | (2,080) |

Year ended

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| | 2004 | 2003 |
|--|----------|---------------------|
| | ----- | ----- |
| | | NIS i (except pe |
| Other than temporary impairment of an investment in an associated company | | |
| Amortization of other than temporary impairment of an investment in an associated company | 1,699 | |
| Applying APB 25 in respect of employee stock options: | | |
| Gross amount | (12,660) | |
| Deferred taxes | 4,202 | |
| | ----- | |
| Net income under U.S. GAAP | 58,720 | |
| | ===== | |
| Earnings per share: | | |
| Under Israeli GAAP - net income per NIS 1 of par value of shares Primary** | 1,544 | |
| | ===== | |
| Under U.S. GAAP - per share: | | |
| Basic | 14.76 | |
| | ===== | |
| Diluted | 14.52 | |
| | ===== | |

* In 2002 including exchange rate differences from the end of the year, to December 31, 2003.

** Each NIS 1 par value is composed of 100 ordinary shares of NIS 0.01 par value.

2) Shareholders' equity:

| | December 31 | |
|---|--------------|-------|
| | 2004 | 2003 |
| | ----- | ----- |
| | In thousands | |
| Shareholders' equity according to Israeli GAAP | 575,313 | 614,2 |
| Effect of treatment of the following items in accordance with US GAAP: | | |
| Functional currency | (47,798) | (57,2 |
| Other than temporary impairment of an investment in an associated company, net of amortization | (15,287) | (16,9 |
| Deferred income taxes | 8,254 | 10,3 |
| | ----- | ----- |
| Shareholders' equity under US GAAP | 520,482 | 550,3 |
| | ===== | ===== |

3) Consolidated balance sheet figures:

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| | D e c e m b e r 3 1 | | |
|---|-----------------------------------|-----------------|-----------------------------------|
| | 2004 | | 2003 |
| | NIS | Re-measured NIS | NIS |
| | In thousands | | |
| | As Reported Under Israeli GAAP | Under U.S. GAAP | As Reported Under Israeli GAAP |
| Assets | | | |
| Inventories | 83,220 | 71,344 | 90,654 |
| Investment in associated companies | 431,752 | 418,787 | 383,879 |
| Fixed assets - net | 324,406 | 285,851 | 325,641 |
| Liabilities and shareholders' equity | | | |
| Deferred taxes - net | 40,693 | 33,132 | 50,789 |
| Shareholders' equity | 575,313 | 520,482 | 614,230 |

j. Statement of cash flows

The Company presents its cash flow information, under Israeli GAAP net of the effects of inflation.

The information to be included under US GAAP for the years ended December 31, 2002, 2003 and 2004 is presented below:

| | 2004 | 2003 |
|---|--------------|-------|
| | NIS | NIS |
| | In thousands | |
| Net cash provided by operating activities | 29,593 | 53,8 |
| Net cash used in investing activities | (42,043) | (32,2 |
| Net cash provided by (used in) financing activities | (138,946) | 125,5 |
| Effect of inflation and exchange difference on cash and cash equivalent | 503 | 5,6 |
| Increase (decrease) in cash and cash equivalents | (150,893) | 152,8 |
| Balance of cash and cash equivalents at beginning of year | 158,706 | 5,9 |

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Balance of cash and cash equivalents
at end of year

| | |
|-------|-------|
| 7,813 | 158,7 |
| ===== | ===== |

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k. Reporting comprehensive Income

In addition to net income, comprehensive income includes translation of foreign currency financial statements of an investee company, as follows:

| | Year Ended December 31 | |
|---|---------------------------------|---------|
| | 2004 | 2003 |
| | Re-measured NIS in thousands | |
| | ----- | ----- |
| Net income under U.S. GAAP | 58,720 | 38,469 |
| Differences from translation of foreign currency financial statements of an investee company | (1,288) | (2,506) |
| Comprehensive income | 57,432 | 35,963 |
| | ===== | ===== |

As of December 31, 2004 the accumulated other comprehensive income aggregates to (1,370) re-measured NIS, in thousands.

Recently issued accounting pronouncements:

1) FAS 123 (revised 2004) Share-based Payment

In December 2004, the Financial Accounting Standards Board ("FASB") issued the revised Statement of Financial Accounting Standards ("FAS") No. 123, Share-Based Payment (FAS 123R), which addresses the accounting for share-based payment transactions in which the Company obtains employee services in exchange for (a) equity instruments of the Company or (b) liabilities that are based on the fair value of the Company's equity instruments or that may be settled by the issuance of such equity instruments. This Statement eliminates the ability to account for employee share-based payment transactions using APB 25, and requires instead that such transactions be accounted for using the grant-date fair value based method. This Statement will be effective as of the beginning of the first annual reporting period that begins after June 15, 2005. Early adoption of FAS 123R is encouraged. The company decided to adopt this statement on January 1, 2006. This Statement applies to all awards granted or modified after the Statement's effective date. In addition, compensation cost for the unvested portion of previously granted awards that remain outstanding on the Statement's effective date shall be recognized on or after the effective date, as the related services are rendered, based on the awards' grant-date fair value as previously calculated for the pro-forma disclosure under FAS 123 (see also c. above).

The Company expects that upon the adoption of FAS 123R, the Company

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will apply the modified prospective application transition method, as permitted by the Statement. Under such transition method, upon the adoption of FAS 123R, the Company's financial statements for periods prior to the effective date of the Statement will not be restated.

The company expects that this statement may have material effect on its financial position and results of operations. The impact of this statement on the Company's financial statements or its results of operations in 2006 and beyond will depend upon various factors, among them the Company's future compensation strategy.

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FAS 151 Inventory Costs - an amendment of ARB 43, Chapter 4

In November 2004, the FASB issued FAS No. 151, "Inventory Costs - an amendment of ARB 43, Chapter 4" (FAS 151). This Statement amends the guidance in ARB No. 43, Chapter 4, "Inventory Pricing," to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material. This Statement requires that those items be recognized as current-period charges. In addition, this Statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. This Statement will be effective for inventory costs incurred during fiscal years beginning after June 15, 2005 (January 1, 2006 for the Company). Earlier application of FAS 151 is permitted. The provisions of this Statement shall be applied prospectively. The Company does not expect this Statement to have a material effect on the Company's financial statements or its results of operations.

FAS 153 Exchanges of Nonmonetary Assets - An Amendment of APB Opinion No. 29

In December 2004, the FASB issued FAS No. 153, Exchanges of Nonmonetary Assets - An Amendment of APB Opinion No. 29 (FAS 153). FAS 153 amends APB Opinion No. 29, Accounting for Nonmonetary Transactions (Opinion 29). The amendments made by FAS 153 are based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the exception for nonmonetary exchanges of similar productive assets and replace it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. The provisions in FAS 153 are effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005 (July 1, 2005 for the Company). Early application of the FAS 153 is permitted. The provisions of this Statement shall be applied prospectively. The Company does not expect the adoption of FAS 153 to have a material effect on the Company's financial statements or its results of operations.

EITF Issue 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments"

In March 2004, the FASB issued EITF Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" which provides new guidance for assessing impairment losses on debt and equity investments. Additionally, EITF Issue No. 03-1 includes new disclosure requirements for investments that are deemed to be temporarily impaired. In September 2004, the FASB delayed the accounting provisions of EITF Issue No. 03-1; however, the disclosure requirements remain effective. The Company will evaluate the effect, if any, of EITF Issue No. 03-1 when final guidance is released

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EITF Issue 02-14, Whether an Investor Should Apply the Equity Method of Accounting to Investments Other Than Common Stock

In July 2004, the FASB issued EITF Issue No. 02-14, "Whether an Investor Should Apply the Equity Method of Accounting to Investments Other Than Common Stock." EITF Issue No. 02-14 addresses whether the equity method of accounting applies when an investor does not have an investment in voting common stock of an investee but exercises significant influence through other means. EITF Issue No. 02-14 states that an investor should only apply the equity method of accounting when it has investments in either common stock or in-substance common stock of the investee, provided that the investor has the ability to exercise significant influence over the operating and financial policies of the investee. The provisions in EITF Issue No. 02-14 are effective for reporting periods beginning after September 15, 2004

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(October 1, 2004 for the Company). The adoption of EITF 02-14 by the Company did not have any effect on the Company's financial statements or its results of operations.

Schedule - Valuation and Qualifying Accounts

Three Years Ended December 31, 2004

(NIS in thousands)

| Column A | Column B | Column C | Column D |
|----------------------------------|-----------------------------------|---|----------|
| | Balance at beginning of period | Additions (reductions) charged to expenses | Deduct |
| | ----- | ----- | ----- |
| Allowance for doubtful accounts: | | | |
| Year ended December 31, 2004 | 13,696 | 3,102 | |
| | ===== | ===== | ===== |
| Year ended December 31, 2003 | 12,752 | 944 | |
| | ===== | ===== | ===== |
| Year ended December 31, 2002 | 11,538 | 1,230 | |
| | ===== | ===== | ===== |

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ITEM 19 - EXHIBITS

(a) The following financial statements and supporting documents are filed with this report:

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- (i) Consolidated Audited Financial Statements of the Company for the year ended December 31, 2004 (including reports of other independent auditors).
 - (ii) Financial statements of Mondi Business Paper Hadera Ltd. for the year ended December 31, 2004.
 - (iii) Financial statements of Hogla-Kimberly Ltd. for the year ended December 31, 2004.
 - (iv) Report of independent accountants on Schedule on Valuation and Qualifying Accounts and Schedule.
 - (v) Report of Independent auditors on reconciliation to U.S. GAAP.
- (b) Exhibits:
- 1.1* Memorandum of Association
 - 1.2** Articles of Association
 - 3.1*** Voting Agreement dated February 5, 1980 by and among Clal Industries Ltd., PEC Israel Economic Corporation and Discount Bank Investment Corporation Ltd.
 - 31.1 Certification of Chief Executive Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to ss. 302 of the Sarbanes-Oxley Act.
 - 31.2 Certification of Chief Financial Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to ss. 302 of the Sarbanes-Oxley Act.
 - 32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C.ss.1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act.
 - 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C.ss.1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act.
- * Previously filed as an exhibit to the Company's Annual Report on Form 20-F for the year ended December 31, 1987, file No. 1-4212, and incorporated by reference herein.
- ** Previously filed as an exhibit to the Company's Annual Report on Form 20-F for the year ended December 31, 2000, file No. 1-4212, filed with the SEC in June 2001 and incorporated by reference herein.
- *** Incorporated by reference to the exhibit number 3.1 in the Company's form 20-F for the year ended December 31, 1987.

SIGNATURES

Pursuant to the requirement of Section 12 of the Securities Exchange Act of 1934, the registrant certifies that it meets all of the requirements for filing on Form 20-F and has duly caused this annual report to be signed on its behalf by the undersigned, thereunto duly authorized.

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AMERICAN ISRAELI PAPER MILLS LIMITED

By: /s/ Lea Katz

Name: Lea Katz
Title: Corporate Secretary

Dated: June 28, 2005

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EXHIBIT INDEX

- 1.1* Memorandum of Association
- 1.2** Articles of Association
- 3.1*** Voting Agreement dated February 5, 1980 by and among Clal Industries Ltd., PEC Israel Economic Corporation and Discount Bank Investment Corporation Ltd. 8.1 List of subsidiaries
- 31.1 Certification of Chief Executive Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to ss. 302 of the Sarbanes-Oxley Act.
- 31.2 Certification of Chief Financial Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to ss. 302 of the Sarbanes-Oxley Act.
- 32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C.ss.1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act.
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C.ss.1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act.
- * Previously filed as an exhibit to the Company's Annual Report on Form 20-F for the year ended December 31, 1987, file No. 1-4212, and incorporated by reference herein.
- ** Previously filed as an exhibit to the Company's Annual Report on Form 20-F for the year ended December 31, 2000, file No. 1-4212, filed with the SEC in June 2001 and incorporated by reference herein.
- *** Incorporated by reference to the exhibit number 3.1 in the Company's form 20-F for the year ended

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EXHIBIT 19(a) (i)

BAR-LEV, MERRARI, GEVA & CO. C.P.A (ISR.)

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ADUITORS' REPORT

To the Shareholders of

EFFEH LANDFILL LTD.

We have audited the balance sheets of EFFEH Landfill Ltd. (hereafter - the Company) as of December 31, 2004 and 2003 and the related statements of operations, changes in shareholders' equity and cash flows for each of the two years in the period ended December 31, 2004. 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.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004 and 2003, and the results of operations and the cash flows for each of the two years in the period ended December 31, 2004, in conformity with generally accepted accounting principles in Israel. Furthermore, in our opinion, the financial statements referred to above are prepared in accordance with the Securities Regulation (Preparation of Annual Financial Statements), 1993.

Accounting principles generally accepted in Israel vary in certain significant respects from accounting principles generally accepted in the United States of America. The application of the latter would have no significant affect the determination of the results of operations for the years ended December 31, 2004 and 2003.

The above opinion is a mere translation of the Hebrew version of the opinion as given in the aforementioned date.

/s/ BAR-LEV, MERRARI, GEVA & CO.
BAR-LEV, MERRARI, GEVA & CO.
Certified Public Accountants (Israel)

Tel Aviv, February 9, 2005

[GRAPHIC OMITTED]

[X] Kost Forer Gabbay & Kasierer
2 Pal-yam
Haifa 33095, Israel

[X] Phone: 972-4-8654000
Fax: 972-4-8654022

REPORT OF INDEPENDENT AUDITORS

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To the Shareholders of

CARMEL CONTAINER SYSTEMS LTD.

We have audited the accompanying consolidated balance sheets of Carmel Container Systems Ltd. ("the Company") and its subsidiaries as of December 31, 2003 and 2004, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of a subsidiary whose assets constitute approximately 10% and 9% of total consolidated assets as of December 31, 2003 and 2004 respectively, and whose revenues constitute approximately 9%, 10% and 8% of total consolidated revenues for the years ended December 31, 2002, 2003 and 2004 respectively. The financial statements of this subsidiary were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to amounts included for this subsidiary is based on the reports of the other auditors.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States) and standards generally accepted in the Israel, including those prescribed by the Israeli 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. 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 audits and the reports of other auditors, the consolidated 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, 2003 and 2004, and the consolidated results of their operations, changes in shareholder's equity and cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in Israel, which differ in certain respects from those generally accepted in the United States (see Note 21 to the consolidated financial statements).

As described in Note 2b, the financial statements as of the dates and for the reported periods subsequent to December 31, 2003, are presented in reported amounts, in conformity with Accounting Standards of the Israel Accounting Standards Board. The financial statements as of the dates and for the reported periods until the aforementioned date are presented in values that were adjusted until that date according to the changes in the general purchasing power of the Israeli currency, in accordance with pronouncements of the Institute of Certified Public Accountants in Israel.

Haifa, Israel,
February 24, 2005

/s/ KOST FORER GABBAY & KASIERER
KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

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[GRAPHIC OMITTED]

| | | | |
|---|------------------------------|---|----------------------|
| X | Kost Forer Gabbay & Kasierer | X | Phone: 972-4-8654000 |
| | 2 Pal-yam | | Fax: 972-4-8654022 |
| | Haifa 33095, Israel | | |

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders of

BARTHELEMI HOLDINGS LTD.

We have audited the accompanying balance sheets of Barthelemi Holdings Ltd. ("the Company") as of December 31, 2004 and 2003 and the consolidated balance sheets as of such dates and the related statements of operations, changes in shareholders' equity and cash flows - of the Company and consolidated - for each of the three years in the period ended December 31, 2004 (not presented separately herein). 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.

We did not audit the financial statements of certain subsidiaries, whose assets included in consolidation constitute approximately 4% of total consolidated assets as of December 31, 2004 and 2003, and whose revenues included in consolidation constitute approximately 6%, 7% and 11% of total consolidated revenues for the years ended December 31, 2004, 2003 and 2002, respectively. Furthermore, we did not audit the financial statements of an affiliate, the investment in which, at equity, amounted to NIS 19,673 thousand and NIS 19,829 thousand as of December 31, 2004 and 2003, respectively, and the Company's equity in its losses amounted to NIS 156 thousand and NIS 14 thousand for the years ended December 31, 2004 and 2003, respectively. The financial statements of those companies were audited by other auditors, whose reports have been furnished to us, and our opinion, insofar as it relates to amounts included for those companies, is based solely on the reports of the other auditors.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position - of the Company and consolidated - as of December 31, 2004 and 2003, and the results of operations, changes in shareholders' equity and cash flows - of the Company and consolidated - for each of the three years in the period ended December 31, 2004, in conformity with generally accepted accounting principles in Israel which differ in certain respects from those generally accepted in the United States, as described in Note 23 to the consolidated financial statements.

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Tel-Aviv, Israel
March 8, 2005

/s/ KOST FORER GABBAY & KASIERER
KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

[LOGO OMITTED]

To the shareholders of
M.M.M United Landfill Industries (1998) Ltd

We have audited the financial statements of M.M.M United Landfill Industries (1998) Ltd. (hereafter - the Company): balance sheets as of December 31, 2004 and 2003 and the related statements of income, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's board of directors and management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004 and 2003 and the results of operations, the changes in shareholders' equity and the cash flows of the Company for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in Israel.

Accounting principles generally accepted in Israel vary in certain significant respects from accounting principles generally accepted in the United States of America. The application of the latter would have no significant affected the determination of the results of operations for the three years in the period ended December 31, 2004.

We draw attention to the said in note 1D regarding the end of the program period (TMA 16A Dudaim Site) in December 31, 2005. The company is currently in procedures to extend the aforementioned program.

The above opinion is a mere translation of the Hebrew version of the opinion as given in the aforementioned date.

/s/ Mualem Glezer Inbar Junio & Co.
Mualem Glezer Inbar Junio & Co.
Certified Public Accountants (Israel)

Ramat-Gan, February 14, 2005

[OBJECT OMITTED]

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders of

TMM INTEGRATED RECYCLING INDUSTRIES LTD.

We have audited the balance sheets of TMM Integrated Recycling Industries Ltd. ("the Company") as of December 31, 2004 and 2003 and the consolidated balance sheets as of such dates and the related statements of operations, changes in shareholders' equity, and cash flows - of the Company and consolidated - for each of the three years in the period ended December 31, 2004 (not presented separately herein). 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.

We did not audit the financial statements of certain subsidiaries, whose assets included in consolidation constitute approximately 4% of total consolidated assets as of December 31, 2004 and 2003, and whose revenues included in consolidation constitute approximately 6%, 7% and 11% of total consolidated revenues for the years ended December 31, 2004, 2003 and 2002, respectively. Furthermore, we did not audit the financial statements of an affiliate, the investment in which, at equity, amounted to NIS 19,673 thousand and NIS 19,829 thousand as of December 31, 2004 and 2003, respectively, and the Company's equity in its losses amounted to NIS 156 thousand and NIS 14 thousand for the years ended December 31, 2004 and 2003, respectively. The financial statements of those companies were audited by other auditors, whose reports have been furnished to us, and our opinion, insofar as it relates to amounts included for those companies, is based solely on the reports of the other auditors.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

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

Tel-Aviv, Israel
March 8, 2005

/s/ KOST FORER GABBAY & KASIERER
KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

AMERICAN ISRAELI PAPER MILLS LIMITED
2004 CONSOLIDATED FINANCIAL STATEMENTS

AMERICAN ISRAELI PAPER MILLS LIMITED
2004 CONSOLIDATED FINANCIAL STATEMENTS

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PricewaterhouseCoopers

Kesselman & Kesselman
Certified Public Accountants
Trade Tower, 25 Hamered Street
Tel Aviv 68125 Israel
P.O Box 452 Tel Aviv 61003
Telephone +972-3-7954555
Facsimile +972-3-7954556

AUDITORS' REPORT

To the shareholders of
AMERICAN ISRAELI PAPER MILLS LIMITED

We have audited the consolidated balance sheets of American Israeli Paper Mills Limited (hereafter - the Company) and its subsidiaries as of December 31, 2004 and 2003 and the related consolidated statements of income, changes in shareholders' equity and cash flows for each of the three years in the period

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ended December 31, 2004. These financial statements are the responsibility of the Company's board of directors and management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

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

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

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

Tel-Aviv, Israel
March 10, 2005

/s/ Kesselman & Kesselman

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

| | | |
|-----------------|---|-------------------------|
| |) | Chairman of the |
| ----- | | |
| Yaki Yerushalmi |) | Board of Directors |
| | | |
| ----- | | |
| Avi brener |) | Chief Executive Officer |
| | | |
| ----- | | |
| Israel Eldar |) | Controller |

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

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

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

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

4

AMERICAN ISRAELI PAPER MILLS LIMITED
CONSOLIDATED STATEMENTS OF INCOME

Note 2004

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

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

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

Share
Capital

Capital
surplus

Curren
adjustm
in res
of fina
stateme
associ
compa

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NIS in thousands

| | | | |
|---|---------|--------|-------|
| BALANCE AT JANUARY 1, 2002 | 125,256 | 90,060 | (3,17 |
| CHANGES IN 2002: | | | |
| Net income | | | |
| Dividend paid | | | |
| Currency adjustments in respect of financial statements of associated companies | | | (30 |
| | ----- | ----- | ----- |
| BALANCE AT DECEMBER 31, 2002 | 125,256 | 90,060 | (3,48 |
| CHANGES IN 2003: | | | |
| Net income | | | |
| Dividend paid | | | |
| Exercise of employee options into shares | 1 | | |
| Currency adjustments in respect of financial statements of associated companies | | | 2,36 |
| | ----- | ----- | ----- |
| BALANCE AT DECEMBER 31, 2003 | 125,257 | 90,060 | (1,12 |
| | ===== | ===== | ===== |
| CHANGES IN 2004: | | | |
| Net income | | | |
| Dividend paid | | | |
| Exercise of employee options into shares | * | | |
| Currency adjustments in respect of financial statements of associated companies | | | (1,68 |
| | ----- | ----- | ----- |
| BALANCE AT DECEMBER 31, 2004 | 125,257 | 90,060 | (2,80 |
| | ===== | ===== | ===== |

*Represents an amount less than NIS 1,000.

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

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(Continued) - 1

AMERICAN ISRAELI PAPER MILLS LIMITED
CONSOLIDATED STATEMENTS OF CASH FLOWS

| | 2004 | 2003 |
|--|---------------------|----------|
| | ----- | ----- |
| | NIS in thousands (s | |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income for the year | 62,732 | 60,047 |
| Adjustments to reconcile net income to net cash provided by operating activities (*) | (15,637) | (7,396) |
| | ----- | ----- |
| Net cash provided by operating activities | 47,095 | 52,651 |
| | ----- | ----- |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchase of fixed assets | (30,952) | (29,247) |
| Short-term investments | (42,000) | (20,000) |

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| | | |
|--|-----------|----------|
| Associated companies: | | |
| Granting of loans | (779) | (8,241) |
| Collection of loans | 13,688 | 21,895 |
| Proceeds from sale of fixed assets | 1,001 | 3,332 |
| | ----- | ----- |
| Net cash used in investing activities | (59,042) | (32,261) |
| | ----- | ----- |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Notes issuance, net of issuance expenses of NIS 800,000 | | 198,909 |
| Consideration in respect of the exercise of options by employees | | 1 |
| Repayment of long-term loans from banks and others | (383) | (762) |
| Redemption of notes | (6,666) | (6,770) |
| Dividend paid | (99,964) | (99,128) |
| Short-term credit from banks - net | (31,933) | 40,606 |
| | ----- | ----- |
| Net cash provided by (used in) financing activities | (138,946) | 132,856 |
| | ----- | ----- |
| INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | (150,893) | 153,246 |
| BALANCE OF CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR | 158,706 | 5,460 |
| | ----- | ----- |
| BALANCE OF CASH AND CASH EQUIVALENTS AT END OF YEAR | 7,813 | 158,706 |
| | ===== | ===== |

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

7

(Concluded) - 2

AMERICAN ISRAELI PAPER MILLS LIMITED
CONSOLIDATED STATEMENTS OF CASH FLOWS

| | | |
|---|--|----------|
| | | 2004 |
| | | ----- |
| | | NIS in |
| (*) Adjustments to reconcile net income to net cash provided by operating activities: Income and expenses not involving cash flows: | | |
| Share in profits of associated companies - net | | (25,072) |
| Dividend received from associated company | | |
| Depreciation and amortization | | 28,633 |
| Deferred income taxes - net | | (10,096) |
| Capital losses (gains) on: | | |
| Sale of fixed assets | | 508 |
| Termination of activities and disposal of assets - net | | |
| Gains on short-term deposits and investments not yet realized | | (464) |
| Linkage and exchange differences on principal of | | |
| long-term loans from banks - net | | (26) |
| Linkage differences on (erosion of) principal of Notes | | 2,184 |
| Erosion of (linkage differences on) principal of | | |
| long-term loans to associated companies | | (721) |
| Appreciation (erosion) of a long-term capital note granted to an associated company | | |

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| | |
|---|---|
| | ----- 5,054 ----- |
| Changes in operating asset and liability items: | |
| Increase in trade receivables | (2,279) |
| Decrease (increase) in other receivables (not include deferred income taxes) | (12,037) |
| Decrease (increase) in inventories | 7,434 |
| Increase (decrease) in trade payables | 2,954 |
| Increase (decrease) in other payables and accruals | (6,655) |
| | ----- (10,583) ----- (15,637) ===== |
| Supplementary cash flow information - cash paid during the year for: | |
| Taxes on income | 3,242 ===== |
| Interest | 20,697 ===== |

Information on activities not involving cash flows:

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

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

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AMERICAN ISRAELI PAPER MILLS LIMITED
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

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

a. General:

1) Activities of the Group

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

2) Use of estimates in the preparation of financial statements

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

3) Definitions:

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

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

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

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AMERICAN ISRAELI PAPER MILLS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

b. Basis of presentation of the financial statements

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

Commencing in 2004, the adjustment of financial statements in Israel for the changes in the exchange rate of the US dollar was discontinued, and transitory provisions for financial reporting on a nominal basis began being applied, as explained below; notwithstanding the above, the comparative figures included in these financial statements are based on the amounts adjusted for the changes in the exchange rate of the US dollar, as previously reported; in the case of the Company, these figures represented adjustment to inflation by way of adjustment of the amounts for the changes in the exchange rate of the US dollar (hereafter - the dollar), see (2) below.

1) Transition to nominal financial reporting in 2004

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

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

Accordingly, the amounts reported in 2004 are composed as follows: amounts originating from the period that preceded the transition date are composed of their adjusted to December 2003 shekel amount, with the addition of amounts in nominal values that were added after the transition date, and net of amounts that were deducted after the transition date (the retirement of such sums is effected at their adjusted values as of transition date, their nominal values, or a combination of the two, according to the circumstances). All the amounts originating from the period after the transition date are included in the financial statements at their nominal values.

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

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

2) Comparative figures - amounts adjusted to end of 2003

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

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

The components of the income statements were, for the most part, adjusted as follows: the components relating to transactions carried out during the reported period - sales, purchases, labor costs, etc. - were adjusted on the basis of the date in which the transaction was carried out, while those relating to non-monetary balance sheet items (mainly - changes in inventories and depreciation) were adjusted on the same basis as the related balance sheet item. The financing component represents financial income and expenses in real terms and the erosion of balances of monetary items during the year.

The investment in some of the associated companies (whose operations constitute an integral part of the Company's operations) and the company's share in their operating results are recorded on the basis of the adjusted financial statements (in accordance with the provisions of Standard No. 12, as

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described above) of these companies. As to associated companies whose financial statements were adjusted until December 31, 2003 on the basis of the changes in the CPI, see (4) below.

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

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

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

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

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

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

c. Principles of consolidation:

- 1) The consolidated financial statements include the accounts of the Company and its subsidiaries. A list of the main subsidiaries is presented in a schedule to the financial statements.
- 2) Intercompany transactions and balances, as well as intercompany profits on sales which have not yet been realized outside the Group, have been eliminated.

d. Inventories

Raw materials and supplies, finished goods, purchased products and maintenance and sundry stores are valued at the lower of cost or market (net of processing costs and after deduction of a

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provision for obsolescence, where appropriate); cost is determined on the moving average basis.

e. Investments in associated companies:

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

f. Marketable securities

These securities are stated at market prices.

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

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

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

g. Fixed assets:

- 1) Fixed assets are stated at cost, net of related investment grants.
- 2) Fixed assets of own manufacture are stated at cost, based on the direct costs with the addition of an appropriate portion of related production costs.
- 3) Borrowing costs in respect of credit applied to finance the construction of the fixed assets - during the period until construction is completed - are charged to cost of such assets.

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- 4) The assets are depreciated by the straight-line method on basis of their estimated useful life, as follows:

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

h. Impairment of Assets

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

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

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

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

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

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

i. Deferred charges

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

j. Deferred income taxes:

- 1) Deferred taxes are computed in respect of differences between the amounts presented in these statements and those

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taken into account for tax purposes. As to the main factors in respect of which deferred taxes have been included - see note 7f. Deferred tax balances are computed at the tax rate expected to be in effect at time of release to income from the deferred tax accounts. The amount of deferred taxes presented in the income statements reflects changes in the above balances during the reporting years.

- 2) Taxes which would apply in the event of disposal of investments in subsidiaries and associated companies have not been taken into account in computing the deferred taxes, as the Company intends to hold these investments, not to realize them.
- 3) The Group may incur an additional tax liability in the event of intercompany dividend distribution derived from "approved enterprises" profits - see note 7a. No account was taken of this additional tax, since it is the Group's policy not to cause distribution of dividend which would involve an additional tax liability to the Group in the foreseeable future.

k. Revenue recognition

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

l. Shipping and handling fees costs

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

m. Allowance for doubtful accounts

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

n. Derivative financial instruments

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

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

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

o. Cash equivalents

The Group considers all highly liquid investments, which include short-term bank deposits that are not restricted as to withdrawal or use, the period to maturity of which did not exceed three

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months at time of deposit, to be cash equivalents.

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

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

- q. Recently issued pronouncement

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

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

NOTE 2 - INVESTMENTS IN ASSOCIATED COMPANIES:

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

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

NOTE 2 - INVESTMENTS IN ASSOCIATED COMPANIES (continued):

- b. Composed as follows:

| | December 31 | |
|--|------------------|---------|
| | 2004 | 2003 |
| | NIS in thousands | |
| Cost: | | |
| Shares | 54,241 | 54,241 |
| Excess of cost of investment - net | 2,086 | 2,086 |
| L e s s - accumulated amortization | (2,624) | (3,068) |
| Gain on issuance of shares of an associated company to a third party | 40,241 | 40,241 |
| Currency adjustments | (2,807) | (1,122) |
| Share in profits accumulated since acquisition - net | 271,492 | 246,864 |

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| | | |
|-------------------------------------|---------|---------|
| | 362,629 | 339,242 |
| Long-term loans and capital notes * | 69,123 | 44,637 |
| | ----- | ----- |
| | 431,752 | 383,879 |
| | ===== | ===== |

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

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

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

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

NOTE 2 - INVESTMENTS IN ASSOCIATED COMPANIES (continued):

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

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

d. Mondy Business Paper Hadera Ltd. (hereafter - Mondy Hadera;

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formerly - Neusiedler Hadera Paper Ltd- NHP):

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

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

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

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

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

NOTE 2 - INVESTMENTS IN ASSOCIATED COMPANIES (continued):

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

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

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

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

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

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

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

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

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

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

NOTE 3 - FIXED ASSETS:

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

| | Cost | | | Balance at end of year |
|---|------------------------------------|---------------------------------|-----------------------------------|------------------------------|
| | Balance at beginning of year | Additions during the year | Retirements during the year | |
| | ----- | ----- | ----- | ----- |
| | NIS in thousands | | | |
| Land and buildings on the land | 185,675 | 3,552 | | 189,227 |
| Machinery and equipment | 653,206 | 25,008 | 4,461 | 673,753 |
| Vehicles | 31,860 | 3,772 | 5,678 | 29,954 |
| Office furniture and equipment (including computers) | 65,569 | 2,800 | 7 | 68,362 |
| Payments on account of machinery and equipment | 17,346 | (4,180) | | 13,166 |
| | ----- | ----- | ----- | ----- |
| | 953,656 | 30,952 | 10,146 | 974,462 |
| | ===== | ===== | ===== | ===== |

Accumulated depreciation

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

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

NOTE 3 - FIXED ASSETS (continued):

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

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

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

- a. Notes

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

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

(1) Series I - May 1992

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

(2) Series II - December 2003

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

b. Other liabilities:

| | December 31 | |
|---|------------------|--------|
| | 2004 | 2003 |
| | NIS in thousands | |
| Capital note to an associated company * | 32,770 | 32,770 |
| Other liability | | 2,243 |
| | ----- | ----- |
| | 32,770 | 35,013 |
| | ===== | ===== |

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

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

NOTE 5 - EMPLOYEE RIGHTS UPON RETIREMENT:

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

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

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

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

NOTE 6 - SHAREHOLDERS' EQUITY:

- a. Share capital

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

| | | December 31 | |
|------------------|------------|-----------------|-----------|
| | | 2004 | 2003 |
| Authorized | | Issued and paid | |
| ----- | | ----- | |
| Number of shares | 20,000,000 | 3,996,674 | 3,968,295 |
| | ===== | ===== | ===== |
| Amount in NIS | 200,000 | 39,967 | 39,683 |
| | ===== | ===== | ===== |

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

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b. Employee stock option plans:

1) The 1998 plan for senior officers in the Group

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

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

NOTE 6 - SHAREHOLDERS' EQUITY (continued):

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

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

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

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

2) The 2001 plan for senior officers in the Group

On April 2, 2001, the Company's board of directors approved a stock option plan for senior officers in the Group (hereafter - the 2001 plan for senior officers). Under this plan, 194,300 options were allotted on July 5, 2001 without consideration. Each option is exercisable in purchase of one ordinary share of NIS 0.01 par value of the Company. The options will be exercisable in four equal annual batches. The blocking period of the first batch is two years, commencing on the date of grant; the blocking period of the second batch is three years from the date of grant, and so forth. Each batch is exercisable within two years from the end of the blocking period.

The exercise price of the options granted as above was set at NIS 217.00, linked to the CPI, on the basis of the CPI as of April 2, 2001. The exercise price for each batch is determined as the lesser of the aforementioned exercise

price or the average price of the Company's shares as quoted on the Tel-Aviv Stock Exchange (hereafter - the Stock Exchange) during thirty trading days preceding to the effective date of each batch, less 10%. As stipulated by the 2001 plan for senior officers, the exercise price is to be adjusted, following dividend distributions. Accordingly, the exercise price as of December 31, 2004 is NIS 177.37 for the first batch, NIS 68.77 for the second batch, NIS 125.18 for the third batch and NIS 177.37 for the fourth batch.

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

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

NOTE 6 - SHAREHOLDERS' EQUITY (continued):

b. Employee stock option plans (continued):

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

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

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

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

This plan is designed to be governed by the terms stipulated by Section 102 of the Israeli Income Tax Ordinance. Inter alia, these terms provide that the company will be allowed to claim, as an expense for tax purposes, the amounts credited to the

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employees as a benefit in respect of shares or options granted under the plan.

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

3) The 2001 employee plan

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

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

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

NOTE 6 - SHAREHOLDERS' EQUITY (continued):

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

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

The fair value of each option - computed on the basis of the Black-Scholes option-pricing model - as prescribed by the regulations of the Tel-Aviv Stock Exchange - was approximately NIS 64.11 on the date of grant.

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

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number of shares the market value of which is equal to the amount of the benefit computed as above. In consideration for the shares, the option holder will pay their par value only.

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

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

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

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

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

NOTE 7 - TAXES ON INCOME:

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

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

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

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

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the income from these enterprises is taxable at the rate of 25% for 3 years.

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

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

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

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

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

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

NOTE 7 - TAXES ON INCOME (continued):

- c. The Law for the Encouragement of Industry (Taxation), 1969

The Company and certain subsidiaries are "industrial companies" as defined by this law. These companies claimed depreciation at accelerated rates on equipment used in industrial activity as stipulated by regulations published under the inflationary adjustments law.

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

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

The income of the Company and its Israeli subsidiaries (other than income from "approved enterprises", see a. below) is taxed

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

e. Carryforward tax losses

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

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

NOTE 7 - TAXES ON INCOME (continued):

f. Deferred income taxes

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

| | Among non-current assets (1) ----- | Among current assets (2) ----- | Among non-current liability (3) ----- |
|------------------------------|---|---|--|
| | NIS in thousands | | |
| Balance at January 1, 2003 | (10,948) | | 58,266 |
| Changes in 2003: | | | |
| Reclassification | 3,885 | (3,885) | |
| Amounts carried to income | (64) | | 3,535 |
| | ----- | ----- | ----- |
| Balance at December 31, 2003 | (7,127) | (3,885) | 61,801 |
| Changes in 2004: | | | |
| Amounts carried to income | 1,769 | (2,626) | (9,239) |
| | ----- | ----- | ----- |
| Balance at December 31, 2004 | (5,358) ===== | (6,511) ===== | 52,562 ===== |

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

(2) In respect of carryforward tax losses.

(3) Mainly in respect of depreciable fixed assets.

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

g. Taxes on income included in the income statements:

1) As follows:

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

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

NOTE 7 - TAXES ON INCOME (continued):

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

| | 2004 ----- | | 2003 ----- | |
|---|---------------|---------------------|---------------|---------------------|
| | % | NIS in thousands | % | NIS in thousands |
| | ----- | ----- | ----- | ----- |
| Income before taxes on income, as reported in the statements of income | 100.0 | 40,812 | 100.0 | 32,204 |
| | ===== | ===== | ===== | ===== |
| Theoretical tax on the above amount | 35.0 | 14,284 | 36.0 | 11,593 |
| Tax benefits arising from reduced tax rate for approved enterprises | | | (1.5) | (487) |
| | ----- | ----- | ----- | ----- |
| | 35.0 | 14,284 | 34.5 | 11,106 |
| Decrease in taxes resulting from computation of deferred taxes at a rate which is different from the theoretical rate | (4.3) | (1,762) | | |

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| | | | | |
|---|--------|---------|-------|---------|
| Tax benefit resulting from changes in tax rates, see d. above | (14.3) | (5,824) | | |
| Tax deduction in respect of options exercised by employees according to section 102 of the Israeli Income Tax Ordinance | (10.3) | (4,221) | (5.0) | (1,607) |
| Other - net | 1.6 | 675 | (5.6) | (1,793) |
| | ----- | ----- | ----- | ----- |
| Taxes on income for the reported year | 7.7 | 3,152 | 23.9 | 7,706 |
| | ===== | ===== | ===== | ===== |

h. Tax assessments

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

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

NOTE 8 - LINKAGE TERMS OF MONETARY BALANCES:

a. As follows:

| | December 31, 2004 | |
|---|---|------------------------------|
| | ----- | ----- |
| | In, or linked to, foreign currency (mainly dollar) | Linked to the Israeli CPI |
| | ----- | ----- |
| | | NIS in thousands |
| Assets: | | |
| Current assets: | | |
| Cash and cash equivalents | 4,531 | |
| Short-term investments | | 45,539 |
| Receivables | 43,600 | 1,799 |
| Investments in associated companies - long-term loans and capital notes | 8,616 | 11,220 |
| | ----- | ----- |
| | 56,747 | 58,558 |
| | ===== | ===== |
| Liabilities: | | |
| Current liabilities: | | |
| Short-term credit from banks | 2,238 | |
| Accounts payables and accruals | 10,100 | 1,013 |
| Long-term liabilities (including current maturities): | | |
| Loans from banks | | |
| Notes | | 235,147 |
| Other liabilities | | |
| | ----- | ----- |
| | 12,338 | 236,160 |

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

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

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

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

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

| | Exchange rate of one dollar | CPI* |
|---------------------|--------------------------------|--------|
| | ----- | ----- |
| | NIS | Points |
| At end of year: | | |
| 2004 | 4.308 | 180.7 |
| 2003 | 4.379 | 178.6 |
| 2002 | 4.737 | 182.0 |
| Change in the year: | | |

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| | | |
|------|--------|--------|
| 2004 | (1.6%) | 1.2% |
| 2003 | (7.6%) | (1.9%) |
| 2002 | 7.3% | 6.5% |

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

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

a. In respect of investment grants

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

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

- b. In 1996, an associated company received a grant amounting to NIS 2,067,000 from the Fund for Preparation for Exposure of the Ministry of Industry and Trade. With respect to this grant, the Company has provided a bank guarantee of NIS 2,036,000 in favor of the State of Israel.
- c. The Company has provided guarantees of NIS 2,154,000 in favor of an associated company, in connection with the latter's participation in a tender. If the associated company does not win the tender, the guarantee will become null and void.
- d. A subsidiary has provided a guarantee of NIS 1,291,000 to a bank in respect of a loan extended to an associated company.
- e. A subsidiary provided guarantees to various entities, in connection with tenders, in the aggregate amount of approximately NIS 1,700,000.

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

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

- f. On May 7, 2001, the Company's board of directors resolved to carry out a plan, which was approved by the shareholders' meeting, to remunerate the Company's chairman of the board of

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directors. According to the plan, a remuneration will be granted, equal to the increase in the value of 50,000 shares of the Company in the period from May 7, 2001 (share price - NIS 194.37, linked to the terms of the plan) to May 7, 2008. The remuneration will be spread over the period commencing two years from the resolution of the board of directors, until the end of seven years from said resolution. In 2004, one quarter of the remuneration was exercised. As of December 31, 2004, another quarter is exercisable. A liability was included in the financial statements in respect of the above plan, under current liabilities.

- g. In accordance with the Companies Law, 1999, in 2004, the Company issued new letters of indemnity to its officers, pursuant to which the Company undertakes to indemnify the officers for any liability or expense, for which indemnification may be paid under the law, that may be incurred by the officers in connection with actions performed by them as part of their duties as officers in the Company, which are directly or indirectly related to the events specified in the addendum to the letters of indemnity, provided that the total amount of indemnification payable to the officers, shall not exceed 25% of the Company's shareholders' equity as per its latest financial statements published prior to the actual indemnification. The liability of officers in connection with the performance of their duties, as above, is partly covered by an insurance policy.

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

NOTE 10 - SUPPLEMENTARY FINANCIAL

STATEMENT INFORMATION:

Balance sheets:

| | Weighted average interest rate at December 31, 2004 ----- |
|--|---|
| a. Short-term investments: | |
| Short term deposit - linked to the CPI | 4.0% |
| Short-term deposit - unlinked | |
| Marketable securities | |
| b. Receivables: | |
| 1) Trade: | |
| Open accounts | |
| Checks collectible | |

The item is:

Net of allowance for doubtful accounts

Includes associated companies

2) Other:

Employees and employee institutions

Associated companies

Prepaid expenses

Advances to suppliers

Deferred income taxes, see note 7f

Income tax authority

Interest receivable

Sundry

c. Inventories:

For industrial activities:

Finished goods

Raw materials and supplies

For commercial activities - purchased products

Maintenance and sundry stores

d. Credit from banks:

| | |
|------------------------------|------|
| Short-term credit - unlinked | 4.5% |
|------------------------------|------|

| | |
|---------------------------------|------|
| Short-term credit - Swiss franc | 3.2% |
|---------------------------------|------|

| | |
|---------------------------------|--|
| Current maturities of long-term | |
|---------------------------------|--|

| | |
|-------|--|
| Loans | |
|-------|--|

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

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

e. Accounts payable and accruals - other:

| December 31 | |
|------------------|-------|
| ----- | ----- |
| 2004 | 2003 |
| ----- | ----- |
| NIS in thousands | |

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

Statements of income:

| | 2004 | 2003 | 2002 |
|--|------------------|---------|---------|
| | ----- | ----- | ----- |
| | NIS in thousands | | |
| f. Sales - net (1): | | | |
| Industrial activities (2) | 363,489 | 326,825 | 310,628 |
| Commercial activities | 119,365 | 138,267 | 145,147 |
| | ----- | ----- | ----- |
| | 482,854 | 465,092 | 455,775 |
| | ===== | ===== | ===== |
| (1) Including sales to associated companies | 121,987 | 115,505 | 104,864 |
| | ===== | ===== | ===== |
| (2) Including sales to export | 42,232 | 44,175 | 40,645 |
| | ===== | ===== | ===== |
| g. Cost of sales: | | | |
| Industrial activities: | | | |
| Materials consumed | 83,533 | 72,292 | 61,649 |
| Payroll and related expenses | 91,468 | 85,419 | 78,903 |
| Depreciation | 24,537 | 22,739 | 21,182 |
| Other manufacturing costs | 82,991 | 80,709 | 77,765 |
| Decrease (increase) in inventory of finished goods | 3,135 | (1,651) | 12,585 |
| | ----- | ----- | ----- |
| | 285,664 | 259,508 | 252,084 |
| Commercial activities - cost of products sold | 90,240 | 102,677 | 111,687 |
| | ----- | ----- | ----- |
| | 375,904 | 362,185 | 363,771 |
| | ===== | ===== | ===== |
| Including purchases from associated Companies | 22,793 | 26,374 | 29,423 |

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| | 2004 ----- | 2003 ----- |
|--|---------------|----------------|
| | | NIS in thous |
| h. Selling, marketing, administrative and general expenses: | | |
| Selling and marketing: | | |
| Payroll and related expenses | 14,311 | 15,225 |
| Packaging, transport and shipping | 6,458 | 5,719 |
| Commissions | 2,467 | 2,733 |
| Depreciation | 1,159 | 1,595 |
| Other | 6,200 | 6,052 |
| | ----- | ----- |
| | 30,595 | 31,324 |
| | ===== | ===== |
| Administrative and general: | | |
| Payroll and related expenses | 36,649 | 36,360 |
| Office supplies, rent and maintenance | 1,521 | 1,938 |
| Professional fees | 1,029 | *1,663 |
| Depreciation | 2,776 | 2,814 |
| Doubtful accounts and bad debts | 3,102 | 944 |
| Other | 1,735 | *4,681 |
| | ----- | ----- |
| | 46,812 | 48,400 |
| L e s s - rent and participation from associated companies | 24,387 | 23,401 |
| | ----- | ----- |
| | 22,425 | 24,999 |
| | ===== | ===== |
| | | |
| | | * Reclassified |
| i. Financial income (expenses) - net*: Expenses: | | |
| In respect of long-term loans - net | 26 | 1,607 |
| In respect of notes - including amortization of deferred charges | 15,188 | 5,031 |
| Erosion of operating monetary balances, net of related hedges | | |
| In respect of short-term balances - net (2002 -net of borrowing costs capitalized to the cost of fixed assets) | 6,547 | 16,917 |
| | ----- | ----- |
| | 21,761 | 23,555 |
| | ----- | ----- |
| Income: | | |
| In respect of long-term loans - net | | |
| In respect of increase in value of operating monetary balances, net of related hedges | 1,901 | **7,429 |
| In respect of short-term balances - net | 6,742 | ** 137 |
| | ----- | ----- |
| | 8,643 | 7,566 |
| | ----- | ----- |
| | (13,118) | (15,989) |
| | ===== | ===== |
| * Including financial income (expenses) in respect of loans to associated companies | 721 | (1,376) |
| | ===== | ===== |

** Reclassified

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

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

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

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

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

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

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

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

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

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

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

NOTE 12 - FINANCIAL INSTRUMENTS AND RISK MANAGEMENT:

- a. Derivative financial instruments

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

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

At the end of 2004, the Company entered into a forward transaction for a period of one year, in order to hedge an amount of NIS 200 million against increases in the CPI, following the termination of the aforementioned transaction in January 2005.

- b. Credit risks

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

Most of these companies sales are made in Israel, to a large

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

c. Fair value of financial instruments

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

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

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

NOTE 13 - INTERESTED PARTIES - TRANSACTIONS AND BALANCES:

a. Transactions:

1) Income (expenses):

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

The amounts presented above represent transactions that the Company carried out in the ordinary course of business with interested parties (companies which are held by the Company's principal shareholder), at terms and prices similar to those applicable to non-affiliated customers and suppliers.

2) Benefits to interested parties:

| | 2004 ----- | 2003 ----- | 2002 ----- |
|---|---------------|---------------|---------------|
| Payroll to interested parties employed By the Company - NIS in thousands | *3,300 | *3,364 | 2,000 |

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| | | | |
|--|-------|-------|-------|
| | ===== | ===== | ===== |
| Number of people to whom the benefits relate | 2 | 2 | 1 |
| | ===== | ===== | ===== |
| Remuneration of directors who are not employed by the Company - NIS in thousands | 528 | 444 | 324 |
| | ===== | ===== | ===== |
| Number of people to whom the benefits relate | 13 | 13 | 9 |
| | ===== | ===== | ===== |

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

- 3) In 2003, an interested party employed by the Company exercised 15,999 options granted to him under the 1998 plan for senior employees. 8,529 shares of NIS 0.01 par value have been issued at par against the exercise of said options.
- 4) As to the plan for the remuneration of the Company's Chairman of the Board of Directors - see note 9f.

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

b. Balances with interested parties:

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

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

NOTE 14 - SEGMENT INFORMATION:

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a. Activities of the Company and its subsidiaries:

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

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

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

NOTE 14 - SEGMENT INFORMATION (continued):

b. Business segment data:

| | Paper and recycling | | | Marke |
|---|---------------------|---------|---------|---------|
| | 2004 | 2003 | 2002 | 2004 |
| | NIS in thousands | | | |
| Sales - net(1) | 367,391 | 332,124 | 314,636 | 115,463 |
| Income (loss) from ordinary operations | 58,496 | 46,282 | 37,488 | (4,566) |
| Financial expenses, net | | | | |
| Other income (expenses) | | | | |
| Income before taxes on income | | | | |
| Segment assets (at end of year) | 494,194 | 497,811 | 482,833 | 56,707 |
| Unallocated assets (at end of year) (2) | | | | |
| Consolidated total assets (at end of year) | | | | |
| Segment liabilities (at end of year) | 66,564 | 58,906 | 66,325 | 20,992 |
| Unallocated liabilities (at end of year) | | | | |
| Consolidated total liabilities (at end of year) | | | | |
| Depreciation and amortization | 26,671 | 25,523 | 24,422 | 1,962 |
| | T o t a l | | | |
| | 2004 | 2003 | 2002 | |
| | NIS in thousands | | | |
| Sales - net(1) | 482,854 | 465,092 | 455,775 | |

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| | | | |
|---|-----------|-----------|-----------|
| Income (loss) from ordinary operations | 53,930 | 46,584 | 36,455 |
| Financial expenses, net | 13,118 | 15,989 | 2,988 |
| Other income (expenses) | | 1,609 | (2,942) |
| Income before taxes on income | 40,812 | 32,204 | 30,525 |
| Segment assets (at end of year) | 550,901 | 557,291 | 548,067 |
| Unallocated assets (at end of year) (2) | 611,486 | 695,983 | 504,056 |
| Consolidated total assets (at end of year) | 1,162,387 | 1,253,274 | 1,052,123 |
| Segment liabilities (at end of year) | 87,566 | 84,602 | 99,255 |
| Unallocated liabilities (at end of year) | 499,518 | 554,442 | 301,918 |
| Consolidated total liabilities (at end of year) | 587,074 | 639,044 | 401,173 |
| Depreciation and amortization | 28,633 | 28,247 | 26,809 |

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

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Schedule

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

Main subsidiaries:

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

Main associated companies:

Hogla-Kimberly Ltd.
 Subsidiaries of Hogla-Kimberly Ltd.:
 Hogla-Kimberly Marketing Limited
 Molett Marketing Limited
 Shikma For Personal Comfort Ltd.

Percent
 indirect
 conf

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Ovisan Sihhi Bez Sanai Ve Ticavet A.S.
Hogla-Kimberly Holdings A.S.
H-K Overseas (Holland) B.V.
Mondy Business Paper Hadera Ltd.
Subsidiaries of Mondy Business Paper Hadera Ltd.:
Grafinir Paper Marketing Ltd.
Yavnir (1999) Ltd.
Mondy Business Paper Hadera Marketing Ltd.
Mitrani Paper Marketing 2000 (1998) Ltd.
Carmel Container Systems Limited
C.D. Packaging Systems Limited*
Barthelemi Holdings Ltd.
T.M.M. Integrated Recycling Industries Ltd.**

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

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

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[GRAPHIC OMITTED]

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

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

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

- Carmel Containers Systems Ltd., according to section 44(c) of the Securities (Periodic and Immediate Reports) Regulations.
- TMM Integrated Recycling Industries Ltd., a reporting corporation.

EXHIBIT 19(a) (ii)

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

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

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

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

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opinion on those financial statements.

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

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

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

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

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

Tel Aviv, February 23, 2005

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

Consolidated

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| | | December 31, | |
|--|------|--------------|-------------|
| | | 2 0 0 4 | 2 0 0 3 |
| | | Reported | Adjusted |
| | Note | Amounts (1) | Amounts (2) |
| | | ----- | ----- |
| Current Assets | | | |
| Cash and cash equivalents | 3 | 10,804 | 31,678 |
| Trade receivables | 4 | 157,815 | 147,748 |
| American Israeli Paper Mills Group, net | | - | - |
| Other receivables | 5 | 7,580 | 11,296 |
| Inventories | 6 | 90,391 | 89,231 |
| | | ----- | ----- |
| | | 266,590 | 279,953 |
| | | ----- | ----- |
| Long-Term Investments | | | |
| Investments in Subsidiaries | 7 | - | - |
| | | ----- | ----- |
| Fixed Assets | | | |
| Cost | 8 | 149,083 | 132,692 |
| Less - accumulated depreciation | | 33,345 | 25,381 |
| | | ----- | ----- |
| | | 115,738 | 107,311 |
| | | ----- | ----- |
| Other Assets - Goodwill | | | |
| | 7B | 3,800 | 4,423 |
| | | ----- | ----- |
| | | 386,128 | 391,687 |
| | | ===== | ===== |
| Current Liabilities | | | |
| Current maturities of long-term | | | |
| bank loans | 11 | 15,125 | 15,108 |
| Trade payables | 9 | 104,661 | 104,097 |
| American Israeli Paper Mills Group, net | | 65,033 | (*) 48,786 |
| Subsidiaries | | - | - |
| Other payables and accrued expenses | 10 | 23,132 | (*) 16,864 |
| | | ----- | ----- |
| | | 207,951 | 184,855 |
| | | ----- | ----- |
| Long-Term Liabilities | | | |
| Long-term bank loans | 11 | 36,248 | 51,725 |
| Capital notes to shareholders | 12 | 17,233 | 43,790 |
| Deferred taxes | 21 | 25,422 | 29,247 |
| Accrued severance pay, net | 13 | 87 | 145 |
| | | ----- | ----- |
| | | 78,990 | 124,907 |
| | | ----- | ----- |
| Commitments and Contingent Liabilities | | | |
| Shareholders' Equity | | | |
| Share capital | 15 | 1 | 1 |
| Premium | | 43,352 | 43,352 |
| Retained earnings | | 55,834 | 38,572 |
| | | ----- | ----- |
| | | 99,187 | 81,925 |
| | | ----- | ----- |
| | | 386,128 | 391,687 |
| | | ===== | ===== |

(*) Reclassified.

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

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

Approval date of the financial statements: February 23, 2005.
 The accompanying notes are an integral part of the financial statements.

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

| | | Consolidated | | | |
|--|------|-------------------------|-------------------------|-------------------------|-------------------|
| | | Year ended December 31, | | | |
| | | 2 0 0 4 | 2 0 0 3 | 2 0 0 2 | 2 0 0 1 |
| | Note | Reported Amounts (1) | Adjusted Amounts (2) | Adjusted Amounts (2) | Report Amounts |
| Net sales | 16 | 686,094 | (*) 640,020 | (*) 574,227 | 482,690 |
| Cost of sales | 17 | 605,738 | 556,890 | (*) 491,712 | 416,500 |
| Gross profit | | 80,356 | 83,130 | 82,515 | 66,190 |
| Selling expenses | 18 | 46,135 | 42,892 | (*) 40,731 | 34,600 |
| General and administrative expenses | 19 | 7,803 | (*) 8,425 | (*) 10,212 | 6,440 |
| Operating profit | | 26,418 | 31,813 | 31,572 | 25,140 |
| Financing expenses, net | 20 | (8,438) | (*) (2,561) | (*) (3,852) | (7,640) |
| Other income (expenses), net | | 100 | (*) (215) | (*) (109) | 400 |
| Income before income taxes | | 18,080 | 29,037 | 27,611 | 17,550 |
| Income taxes | 21 | 818 | 10,518 | 11,534 | 3500 |
| Income after income taxes | | 17,262 | 18,519 | 16,077 | 17,190 |
| Equity in net earnings (losses) of Subsidiaries | | - | - | - | 700 |
| Net income for the year | | 17,262 | 18,519 | 16,077 | 17,260 |

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| | | | | |
|-----------------------------|--------|--------|--------|--------|
| Earnings per share (in NIS) | 17,262 | 18,519 | 16,077 | 17,262 |
| | ===== | ===== | ===== | ===== |
| Number of shares used | | | | |
| In computation | 1,000 | 1,000 | 1,000 | 1,000 |
| | ===== | ===== | ===== | ===== |

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

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

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

| | Share capital | Premium | Retain earnin |
|-----------------------------|------------------|---------|------------------|
| | ----- | ----- | ----- |
| Balance - January 1, 2002 | | | |
| (Adjusted Amounts (2)) | 1 | 43,352 | 3,977 |
| Changes during 2002: | | | |
| Net income for the year | - | - | 16,077 |
| | ----- | ----- | ----- |
| Balance - December 31, 2002 | | | |
| (Adjusted Amounts (2)) | 1 | 43,352 | 20,054 |
| Changes during 2003: | | | |
| Net income for the year | - | - | 18,519 |
| | ----- | ----- | ----- |
| Balance - December 31, 2003 | | | |
| (Adjusted Amounts (2)) | 1 | 43,352 | 38,573 |
| Changes during 2004: | | | |
| Net income for the year | - | - | 17,262 |
| | ----- | ----- | ----- |
| Balance - December 31, 2004 | | | |
| (Reported Amounts (1)) | 1 | 43,352 | 55,835 |
| | ===== | ===== | ===== |

- (1) See Note 2A.

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

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

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

| | Consolidated | | | 2 0 0 4 Reported Amounts (1) |
|--|-------------------------|----------|----------|------------------------------------|
| | Year ended December 31, | | | |
| | 2 0 0 4 | 2 0 0 3 | 2 0 0 2 | |
| | | | | 2 0 0 4 Reported Amounts (1) |
| Cash flows - operating activities | | | | |
| Net income for the year | 17,262 | 18,519 | 16,077 | 17,262 |
| Adjustments to reconcile net income to net cash provided by operating activities (Appendix A) | 20,295 | 37,698 | 31,659 | 30,855 |
| Net cash provided by operating activities | 37,557 | 56,217 | 47,736 | 48,117 |
| Cash flows - investing activities | | | | |
| Acquisition of fixed assets | (16,235) | (9,339) | (16,305) | (16,235) |
| Proceeds from sale of fixed assets | 197 | 635 | 800 | 93 |
| Net cash used in investing activities | (16,038) | (8,704) | (15,505) | (16,142) |
| Cash flows - financing activities | | | | |
| Short-term bank credit, net | - | (18) | (4,147) | - |
| Repayment of long-term loans | (15,265) | (21,116) | (7,266) | (15,265) |
| Repayment of long-term capital notes to shareholders | (27,128) | (43,790) | - | (27,128) |
| Net cash used in financing activities | (42,393) | (64,924) | (11,413) | (42,393) |
| Increase (decrease) in cash and cash equivalents | (20,874) | (17,411) | 20,818 | (10,418) |
| Cash and cash equivalents - beginning of year | 31,678 | 49,089 | 28,271 | 20,034 |

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| | | | | |
|--|-----------------|-----------------|-----------------|----------------|
| Cash and cash equivalents - end of year | 10,804 ===== | 31,678 ===== | 49,089 ===== | 9,616 ===== |
|--|-----------------|-----------------|-----------------|----------------|

(1) See Note 2A.

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

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

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

| | Consolidated | | | |
|---|-------------------------|-------------------------|-------------------------|-------------------------|
| | Year ended December 31, | | | Year |
| | 2 0 0 4 | 2 0 0 3 | 2 0 0 2 | 2 0 0 4 |
| | Reported Amounts (1) | Adjusted Amounts (2) | Adjusted Amounts (2) | Reported Amounts (1) |
| A. Adjustments to reconcile net income to net cash provided by operating activities | | | | |
| Income and expenses items not involving cash flows: | | | | |
| Equity in net losses (earnings) of subsidiaries | - | - | - | (71) |
| Depreciation and amortization | 9,118 | 8,626 | 8,077 | 7,885 |
| Deferred taxes, net | 823 | 10,438 | 11,483 | 359 |
| Increase (decrease) in liability for severance pay, net | (58) | 14 | 5 | (58) |
| Capital loss (gain) from sale of fixed assets | (100) | 215 | 84 | (47) |
| Effect of exchange rate and linkage differences of long-term bank loans and long-term loan to subsidiary | (195) | 1,460 | (134) | (195) |
| Effect of exchange rate differences of long-term capital notes to shareholders | 571 | - | - | 571 |
| Changes in assets and liabilities: | | | | |
| Decrease (increase) in trade receivables | (10,067) | 7,247 | (696) | - |
| Decrease (increase) | | | | |

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| | | | | |
|--|---------|-------------|--------------|----------|
| in other receivables | (932) | 752 | 9,025 | 574 |
| Decrease (increase) | | | | |
| in inventories | (1,160) | (9,533) | 13,010 | 2,349 |
| Increase (decrease) in trade payables | (220) | 27,447 | 6,043 | 9,721 |
| Increase (decrease) in American Israeli Paper Mills Group, net | 16,247 | (*) (1,612) | (*) (19,014) | (39,448) |
| Increase in Subsidiaries | - | - | - | 48,966 |
| Increase (decrease) in other Payables and accrued expenses | 6,268 | (*) (7,356) | (*) 3,776 | 249 |
| | ----- | ----- | ----- | ----- |
| | 20,295 | 37,698 | 31,659 | 30,855 |
| | ===== | ===== | ===== | ===== |
| B. Non-cash activities Acquisition of fixed assets on credit | 784 | - | - | 784 |
| | ===== | ===== | ===== | ===== |

(*) Reclassified.

(1) See Note 2A.

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

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

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

NOTE 1 - DESCRIPTION OF BUSINESS AND GENERAL

A. Description of Business

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

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

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

The Company is presently owned by NAG (50.1%) and American-Israeli

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Paper Mills Ltd. ("AIPM") (49.9%).

B. Definitions:

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

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MONDI BUSINESS PAPER HADERA LTD.
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NOTES TO FINANCIAL STATEMENTS

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

C. Use of Estimates

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

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

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

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

(1) Definitions

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

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

(2) General

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

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

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

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

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MONDI BUSINESS PAPER HADERA LTD.
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NOTES TO FINANCIAL STATEMENTS

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

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

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

a. Balance Sheet Items

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

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

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

b. Statement of Operations Items

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

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

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

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

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MONDI BUSINESS PAPER HADERA LTD.
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NOTES TO FINANCIAL STATEMENTS

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

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

(4) Principles of Adjustment applicable for financial statements relating to reporting periods ended through December, 31 2004

a. Balance Sheet Items

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

Monetary items (items whose balance sheet amount reflects their

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

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

b. Statement of Operations Items

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

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

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

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MONDI BUSINESS PAPER HADERA LTD.
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NOTES TO FINANCIAL STATEMENTS

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

B. Principles of Consolidation

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

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

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

C. Cash and Cash Equivalents

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

D. Allowance for Doubtful Accounts

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

E. Inventories

Inventories are stated at the lower of cost or market value. Cost is determined for raw materials, auxiliary materials and finished

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products on the basis of weighted moving average cost per unit.

F. Investments in Subsidiaries

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

G. Fixed Assets

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

The annual depreciation and amortization rates are: %

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

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MONDI BUSINESS PAPER HADERA LTD.
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NOTES TO FINANCIAL STATEMENTS

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

G. Fixed Assets (cont.)

Impairment of Long-Lived Assets

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

H. Other Assets - Goodwill

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

In March 2004, the Israeli Accounting Standards Board issued Standard

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

I. Supplier Discounts

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

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NOTES TO FINANCIAL STATEMENTS

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

J. Deferred Income Taxes

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

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

K. Revenue Recognition

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

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is recorded when revenues are recognized.

L. Forward Transactions

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

M. Earnings Per Share

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

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MONDI BUSINESS PAPER HADERA LTD.
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NOTES TO FINANCIAL STATEMENTS

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

N. Exchange Rates and Linkage Basis

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

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

| As of: | Representative exchange rate of the Dollar (NIS per \$1) | CPI "in respect of" (in points) |
|---|---|---------------------------------------|
| | ----- | ----- |
| December 31, 2004 | 4.308 | 180.74 |
| December 31, 2003 | 4.379 | 178.58 |
| December 31, 2002 | 4.737 | 182.02 |
| | | |
| Increase (decrease) during the year ended: | % | % |
| | - | - |
| December 31, 2004 | (1.6) | 1.2 |
| December 31, 2003 | (7.6) | (1.9) |
| December 31, 2002 | 7.3 | 6.5 |

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

O. Reclassification

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

P. Recent Accounting Standards - Income Taxes

In July 2004, the Israeli Accounting Standards Board published

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

NOTE 3 - CASH AND CASH EQUIVALENTS

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

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MONDI BUSINESS PAPER HADERA LTD.
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NOTES TO FINANCIAL STATEMENTS

NOTE 4 - TRADE RECEIVABLES

| | Consolidated | |
|-------------------|---------------------|---------------------|
| | December 31, | |
| | 2 0 0 4 | 2 0 0 3 |
| | Reported Amounts | Adjusted Amounts |
| | NIS in thousands | |
| Composition: | | |
| Domestic | | |
| Open accounts | 107,693 | 96,469 |
| Checks receivable | 29,943 | 35,952 |
| | 137,636 | 132,421 |
| | ===== | ===== |
| Foreign | | |

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| | | |
|--|---------|---------|
| Open accounts | 749 | - |
| Related parties | 21,872 | 18,957 |
| | ----- | ----- |
| | 22,621 | 18,957 |
| | ----- | ----- |
| Less - allowance for doubtful accounts | 2,442 | 3,630 |
| | ----- | ----- |
| | 157,815 | 147,748 |
| | ===== | ===== |

NOTE 5 - OTHER RECEIVABLES

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

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MONDI BUSINESS PAPER HADERA LTD.
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NOTES TO FINANCIAL STATEMENTS

NOTE 6 - INVENTORIES

| | Consolidated | |
|-----------------------------|------------------|----------|
| | ----- | |
| | December | |
| | ----- | |
| | 2 0 0 4 | 2 0 0 3 |
| | ----- | ----- |
| | Reported | Adjusted |
| | Amounts | Amounts |
| | ----- | ----- |
| | NIS in thousands | |
| Raw and auxiliary materials | 30,098 | 31,389 |
| Finished products (1) | 60,293 | 57,842 |
| | ----- | ----- |
| | 90,391 | 89,231 |

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| | | |
|--|-------|-------|
| | ===== | ===== |
| (1) Includes products in transit | 1,723 | - |
| | ===== | ===== |
| The inventories are net of provision for obsolescence | 1,302 | 1,347 |
| | ===== | ===== |

NOTE 7 - INVESTMENTS IN SUBSIDIARIES

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

Long-term loan (*)

(*) The non-interest bearing loan, denominated in NIS and linked to the Israeli Consumer Price Index, was considered part of the Company's investments in the Subsidiary. The loan was repaid at the end of 2004.

B. Goodwill: NIS in thousands

Cost
 Less - accumulated amortization

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C. Consolidated Subsidiaries

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

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

NOTE 8 - FIXED ASSETS

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

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| | | | |
|--------------------|-------|---------|-------|
| (Adjusted Amounts) | 2,297 | 102,687 | 570 |
| | ===== | ===== | ===== |

(*) Reclassified.

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MONDI BUSINESS PAPER HADERA LTD.
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NOTES TO FINANCIAL STATEMENTS

NOTE 8 - FIXED ASSETS (cont.)

| Company | Leasehold improvements | Machinery and equipment | Motor vehicles | Office furniture and equipment |
|---|---------------------------|-------------------------------|-------------------|---|
| | ----- | ----- | ----- | ----- |
| | NIS in thousands | | | |
| Cost: | | | | |
| Balance - January 1, 2004 (Adjusted Amounts) | 2,651 | (*)123,066 | 71 | 1,829 |
| Changes during 2004: | | | | |
| Additions | - | 16,155 | 811 | 53 |
| Dispositions | - | (317) | (7) | - |
| | ----- | ----- | ----- | ----- |
| Balance - December 31, 2004 (Reported Amounts) (1) | 2,651 | 138,904 | 875 | 1,882 |
| | ----- | ----- | ----- | ----- |
| Accumulated depreciation: | | | | |
| Balance - January 1, 2004 (Adjusted Amounts) | 1,040 | 21,033 | 38 | 590 |
| Changes during 2004: | | | | |
| Additions | 265 | 7,172 | 121 | 327 |
| Dispositions | - | (277) | (1) | - |
| | ----- | ----- | ----- | ----- |
| Balance - December 31, 2004 (Reported Amounts) | 1,305 | 27,928 | 158 | 917 |
| | ----- | ----- | ----- | ----- |
| Net book value: | | | | |
| December 31, 2004 (Reported Amounts) | 1,346 | 110,976 | 717 | 965 |
| | ===== | ===== | ===== | ===== |
| December 31, 2003 (Adjusted Amounts) | 1,611 | 102,033 | 33 | 1,239 |
| | ===== | ===== | ===== | ===== |

(*) Reclassified.

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

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NOTES TO FINANCIAL STATEMENTS

NOTE 9 - TRADE PAYABLES

| | Consolidated | |
|---------------------------------------|---------------------|---------------------|
| | December 31 | |
| | 2 0 0 4 | 2 0 0 3 |
| | Reported Amounts | Adjusted Amounts |
| | NIS in thousands | |
| In Israeli currency | 22,484 | 19,981 |
| In foreign currency or linked thereto | 82,177 | 84,116 |
| | 104,661 | 104,097 |
| | ===== | ===== |

NOTE 10 - OTHER PAYABLES AND ACCRUED EXPENSES

| | Consolidated | |
|---|---------------------|---------------------|
| | December 31 | |
| | 2 0 0 4 | 2 0 0 3 |
| | Reported Amounts | Adjusted Amounts |
| | NIS in thousands | |
| Accrued payroll and related expenses | 11,703 | (*) 11,900 |
| Value Added Tax | 3,366 | 368 |
| Advances from customers | 862 | 258 |
| NAG - Parent Company | 2,252 | 552 |
| Interest payable | 2,900 | 2,882 |
| Forward transaction | 1,322 | - |
| Other | 727 | (*) 904 |
| | 23,132 | (*) 16,864 |
| | ===== | ===== |

(*) Reclassified.

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NOTES TO FINANCIAL STATEMENTS

NOTE 11 - LONG-TERM BANK LOANS

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

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

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

B. Maturities

| | |
|----------------------------------|-----|
| Second year - 2006 | 15 |
| Third year - 2007 | 11 |
| Fourth year - 2008 | 3 |
| Fifth year - 2009 | 5 |
| Sixth year - 2010 and thereafter | --- |
| | 36 |
| | === |

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

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December 31, 2004, the Company was in full compliance with the covenants stipulated in the bank agreements and this financial ratio amounted to 30.15%.

- D. As to a "negative pledge agreement" signed by the Company, see Note 14B.
- E. In 2004 and 2003, the Company and its Subsidiaries entered into an agreement for a bank credit facility, pursuant to which the Company and its subsidiaries may, from time to time, borrow an aggregate principal amount of up to adjusted NIS 87,580 thousand. Under the

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NOTES TO FINANCIAL STATEMENTS

terms of the agreement, the credit facility has no time limit. As of the balance sheet date, the Group has not utilized any of the credit facility.

NOTE 12 - CAPITAL NOTES TO SHAREHOLDERS

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

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

NOTE 13 - ACCRUED SEVERANCE PAY, NET

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

NOTE 14 - COMMITMENTS AND CONTINGENT LIABILITIES

A. Commitments

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

Consolidated Company

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

B. Liens

To secure long-term bank loans and short-term bank credit (the balance of which as of December, 31 2004 is NIS 51,373 thousand), the Company entered into a "negative pledge" agreement under which the Company is committed not to pledge any of its assets, excluding fixed pledges relating to assets financed by others, prior to the consent of the banks.

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NOTES TO FINANCIAL STATEMENTS

NOTE 14 - COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

C. Guarantees

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

NOTE 15 - SHARE CAPITAL

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

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

NOTE 16 - NET SALES

| Consolidated | | | |
|-------------------------|----------|----------|----------|
| Year ended December 31, | | | |
| ----- | ----- | ----- | ----- |
| 2 0 0 4 | 2 0 0 3 | 2 0 0 2 | 2 0 0 4 |
| ----- | ----- | ----- | ----- |
| Reported | Adjusted | Adjusted | Reported |
| Amounts | Amounts | Amounts | Amounts |
| ----- | ----- | ----- | ----- |

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NIS in thousands

| | | | | |
|-----------------------|---------|-------------|-------------|---------|
| Industrial operations | 471,190 | (*) 453,807 | (*) 422,885 | 482,698 |
| Commercial operations | 214,904 | 186,213 | (*) 151,342 | - |
| | ----- | ----- | ----- | ----- |
| | 686,094 | (*) 640,020 | (*) 574,227 | 482,698 |
| | ===== | ===== | ===== | ===== |

(*) Reclassified.

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

NOTE 17 - COST OF SALES

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

(*) Reclassified.

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

NOTE 18 - SELLING EXPENSES

| | Consolidated | | Year ended December 31, |
|--|----------------------------|----------------------------|----------------------------|
| | Year ended December 31, | | |
| | Year ended December 31, | Year ended December 31, | |

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| | 2 0 0 4 ----- Reported Amounts ----- | 2 0 0 3 ----- Adjusted Amounts ----- | 2 0 0 2 ----- Adjusted Amounts ----- | 2 0 0 4 ----- Reported Amounts ----- |
|--|--|--|--|--|
| | NIS in thousands | | | NIS |
| Salaries and related expenses | 17,169 | 16,913 | (*) 16,440 | 17,169 |
| Packaging and shipping to customers | 16,235 | (*) 14,368 | (*) 14,460 | 15,464 |
| Maintenance and rent | 7,973 | (*) 7,641 | (*) 7,195 | 313 |
| Transportation expenses | 1,256 | 1,178 | 1,427 | 1,137 |
| Advertising | - | 180 | 153 | - |
| Commissions and license fees to a shareholder | 2,912 | 1,865 | 176 | - |
| Depreciation | 552 | 670 | 880 | 523 |
| Other | 38 | (*) 77 | (*) - | - |
| | ----- 46,135 ===== | ----- 42,892 ===== | ----- (*) 40,731 ===== | ----- 34,606 ===== |

(*) Reclassified.

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

NOTE 19 - GENERAL AND ADMINISTRATIVE EXPENSES

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

(*) Reclassified.

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NOTE 20 - FINANCING EXPENSES, NET

| | Consolidated | | | Year ended December 31, 2 0 0 4 (*) |
|---|-------------------------|---------------------|---------------------|--|
| | Year ended December 31, | | | |
| | 2 0 0 4 | (*) 2 0 0 3 | (*) 2 0 0 2 | |
| | Reported Amounts | Adjusted Amounts | Adjusted Amounts | |
| | NIS in thousands | | | NIS |
| Interest on long-term bank loans | 2,573 | 3,254 | 4,208 | 2,573 |
| Erosion of monetary assets and liabilities, net | 2,070 | (783) | (1,210) | 1,293 |
| Forward transaction | 1,322 | - | - | 1,322 |

(*) Reclassified.

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

NOTE 21 - INCOME TAXES

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

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

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818 10,518 11,534 359
 === ===== ===== ===

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

| | Consolidated | | | |
|---|-------------------------|-------------|-------------|----------|
| | Year ended December 31, | | | |
| | 2 0 0 4 | (*) 2 0 0 3 | (*) 2 0 0 2 | 2 0 0 4 |
| | Reported | Adjusted | Adjusted | Reported |
| | Amounts | Amounts | Amounts | Amounts |
| | NIS in thousands | | | |
| Income before income taxes | 18,080 | 29,037 | 27,611 | 17,550 |
| | ===== | ===== | ===== | ===== |
| Tax computed by statutory tax rate (35%-36% - see E. below) | 6,328 | 10,453 | 9,940 | 6,143 |
| Tax increments (savings) due to: | | | | |
| Non-deductible expenses | 211 | 226 | 239 | - |
| Non-taxable income | (40) | - | (94) | (21) |
| Reduction in corporate tax rates - (E. below) | (4,397) | - | - | (4,479) |
| Differences arising from basis of measurement (**) | (1,198) | (161) | 1,449 | (1,284) |
| Prior years income taxes | (86) | - | - | - |
| | ----- | ----- | ----- | ----- |
| | 818 | 10,518 | 11,534 | 359 |
| | ===== | ===== | ===== | ===== |

(*) Reclassified.

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

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

NOTE 21 - INCOME TAXES (cont.)

D. Deferred Taxes

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| | Consolidated | | | |
|---|-------------------------|---------------------|---------------------|---------------------|
| | Year ended December 31, | | | Year |
| | 2 0 0 4 | 2 0 0 3 | 2 0 0 2 | 2 0 0 4 |
| | Reported Amounts | Adjusted Amounts | Adjusted Amounts | Reported Amounts |
| | NIS in thousands | | | |
| Balance as of beginning of year | (20,647) | (10,209) | 1,274 | (22,135) |
| Changes during the year | (5,220) | (10,438) | (11,483) | (4,838) |
| Adjustment due to change in income tax rates | 4,397 | - | - | 4,479 |
| Balance as of end of year | (21,470) | (20,647) | (10,209) | (22,494) |

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

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

For 2003 - Deferred taxes were computed at 36%.

E. Reduction of Corporate Tax Rates

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

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

NOTE 21 - INCOME TAXES (cont.)

- F. Carryforward tax losses of the Group and the Company are NIS 4,362 thousand and NIS 4,010 thousand as of December 31, 2004, respectively.
- G. The Company and its Subsidiaries have tax assessments that are considered final through the 2000 tax year.

NOTE 22 - RELATED PARTIES AND INTERESTED PARTIES

- A. Balances with Related Parties and Subsidiaries

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

(*) Reclassified.

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

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

B. Transactions with Related Parties and Subsidiaries

| | Consolidated | | | Comp | |
|--|-------------------------|---------------------|---------------------|------------------|---------|
| | Year ended December 31, | | | Year ended D | |
| | 2 0 0 4 | 2 0 0 3 | 2 0 0 2 | 2 0 0 4 | 2 0 0 |
| Reported Amounts | Adjusted Amounts | Adjusted Amounts | Reported Amounts | Adjust Amount | |
| NIS in thousands | | | NIS in th | | |
| Sales to related parties | 165,596 | 171,131 | 155,599 | - | |
| Sales to Subsidiaries | - | - | - | 482,698 | 462, |
| Cost of sales | 106,546 | (*) 88,613 | (*) 75,716 | 78,400 | (*) 73, |
| Selling expenses, net (Participation in selling expenses, net) | 9,875 | (*) 6,428 | (*) - | 1,796 | (*) (1, |
| General and administrative expenses | 1,837 | (*) 1,410 | (*) 1,756 | 1,480 | (*) 1, |
| Financing expenses (income), net | 1,939 | 13,759 | (3,722) | 2,268 | |

(*) Reclassified.

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

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

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

NOTE 23 - DISCLOSURE AND PRESENTATION OF FINANCIAL INSTRUMENTS

A. Credit Risk

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

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

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

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

B. Fair Value of Financial Instruments

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

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

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

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

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

NOTE 24 - COMPANY'S FINANCIAL STATEMENTS IN NOMINAL VALUES

A. Balance Sheets

| | Compl ----- Decemb ----- 2 0 0 4 ----- NIS in t |
|---|---|
| Current Assets | |
| Cash and cash equivalents | 9,616 |
| American Israeli Paper Mills Group, net | 178,289 |

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| | |
|--|---------|
| Other receivables | 5,772 |
| Inventories | 60,301 |
| | ----- |
| | 253,978 |
| | ----- |
| Long-Term Investments | |
| Investments in Subsidiaries | 648 |
| | ===== |
| Fixed Assets, net | 111,066 |
| | ----- |
| | 365,692 |
| | ===== |
| Current Liabilities | |
| Current maturities of long-term bank loans | 15,125 |
| Trade payables | 63,902 |
| Subsidiaries | 99,159 |
| Other payables and accrued expenses | 16,480 |
| | ----- |
| | 194,666 |
| | ----- |
| Long term liabilities | |
| Long term-bank loans | 36,248 |
| Capital notes to shareholders | 17,233 |
| Accrued severance pay, net | 87 |
| | ----- |
| | 53,568 |
| | ----- |
| Shareholders' Equity | 117,458 |
| | ----- |
| | 365,692 |
| | ===== |

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

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

B. Statement of Operations

| | Year ended December 31, | | |
|---------------|-------------------------|---------|-------------|
| | 2 0 0 4 | 2 0 0 3 | 2 0 0 2 |
| | ----- | ----- | ----- |
| | NIS in thousands | | |
| Net sales | 482,698 | 480,764 | 452,986 |
| Cost of sales | 417,831 | 406,930 | (*) 380,830 |
| | ----- | ----- | ----- |

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| | | | |
|---|---------|-----------|------------|
| Gross profit | 64,867 | 73,834 | 72,156 |
| Selling expenses | 34,598 | 33,455 | (*) 26,929 |
| General and administrative expenses | 6,444 | (*) 9,080 | (*) 4,629 |
| | ----- | ----- | ----- |
| Operating profit | 23,825 | 31,299 | 40,598 |
| Financing (expenses) income, net | (7,143) | 3,152 | (11,957) |
| Other income (expenses), net | 48 | (*) (93) | (*) (10) |
| | ----- | ----- | ----- |
| Income before income taxes | 16,730 | 34,358 | 28,631 |
| Income taxes | - | - | - |
| | ----- | ----- | ----- |
| Income after income taxes | 16,730 | 34,358 | 28,631 |
| Equity in net earnings (losses) of Subsidiaries | 272 | (34) | (385) |
| | ----- | ----- | ----- |
| Net income for the year | 17,002 | 34,324 | 28,246 |

(*) Reclassified.

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

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

C. Statements of Changes in Shareholders' Equity

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

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| | | | |
|-----------------------------|-------|--------|--------|
| Net income for the year | - | - | 17,002 |
| | ----- | ----- | ----- |
| Balance - December 31, 2004 | 1 | 41,125 | 76,332 |
| | ===== | ===== | ===== |

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EXHIBIT 19(a) (iii)

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

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

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders of
Hogla-Kimberly Ltd.

We have audited the accompanying balance sheets of Hogla-Kimberly Ltd. ("the Company") as of December 31, 2004 and 2003, and the consolidated balance sheets as of those dates, and the related statements of operations, changes in shareholders' equity and cash flows - of the Company and on a consolidated basis

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- for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's Board of Directors and management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

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

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

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

Tel Aviv, March 7, 2005

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

| | Consolidated | |
|------|--------------|----------|
| | December 31, | |
| Note | 2 0 0 4 | 2 0 0 3 |
| ---- | ----- | ----- |
| | Reported | Adjusted |

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| | | Amounts (1) | Amounts (3) |
|---|----|-------------|-------------|
| | | ----- | ----- |
| Current Assets | | | |
| Cash and cash equivalents | 3 | 117,364 | 37,340 |
| Current maturities of long-term bank deposits | 7 | - | 7,882 |
| Trade receivables | 4 | 214,389 | 229,979 |
| Other receivables | 5 | 35,725 | 14,222 |
| Inventories | 6 | 142,551 | 92,664 |
| | | ----- | ----- |
| | | 510,029 | 382,087 |
| | | ----- | ----- |
| Long-Term Investments | | | |
| Long-term bank deposits | 7 | 68,928 | 70,064 |
| Capital note of shareholder | 8 | 32,770 | 32,770 |
| Investments in Subsidiaries | 9 | - | - |
| | | ----- | ----- |
| | | 101,698 | 102,834 |
| | | ----- | ----- |
| Fixed Assets | 10 | | |
| Cost | | 507,175 | 479,744 |
| Less - accumulated depreciation | | 222,256 | 210,176 |
| | | ----- | ----- |
| | | 284,919 | 269,568 |
| | | ----- | ----- |
| Other Assets | | | |
| Goodwill | 9B | 25,878 | 29,073 |
| Deferred taxes | 22 | 15,108 | - |
| | | ----- | ----- |
| | | 40,986 | 29,073 |
| | | ----- | ----- |
| | | 937,632 | 783,562 |
| | | ===== | ===== |
| Current Liabilities | | | |
| Short-term bank credit | | - | 1,087 |
| Current maturities of | | | |
| long-term bank loans | 13 | 68,747 | 15,147 |
| Trade payables | 11 | 219,902 | 139,555 |
| Other payables and accrued expenses | 12 | 38,720 | 37,632 |
| | | ----- | ----- |
| | | 327,369 | 193,421 |
| | | ----- | ----- |
| Long-Term Liabilities | | | |
| Long-term bank loans | 13 | 81,851 | 96,338 |
| Deferred taxes | 22 | 37,388 | 29,428 |
| | | ----- | ----- |
| | | 119,239 | 125,766 |
| | | ----- | ----- |
| Commitments and Contingent Liabilities | 15 | | |
| Minority Interest | | 54,492 | 51,394 |
| | | ----- | ----- |
| Shareholders' Equity | | | |
| Share capital | 16 | 29,038 | 28,788 |
| Capital reserves | | 180,414 | 156,799 |
| Translation adjustments relating to | | | |
| foreign held autonomous Subsidiary (2) | | (3,377) | - |
| Retained earnings | | 230,457 | 227,394 |
| | | ----- | ----- |
| | | 436,532 | 412,981 |
| | | ----- | ----- |
| | | 937,632 | 783,562 |
| | | ===== | ===== |

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

 T. Davis
 Chairman of the Board of Directors

 Y. Yerushalmi
 Vice-Chairman of the Board of Directors

 O. Argov
 Chief Financial Officer

 A. Brenner
 Chief Executive Officer

 Approval date of the financial statements: March 7, 2005.
 The accompanying notes are an integral part of the financial statements.

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

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

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| | | | | |
|--|-----------|-----------|-----------|-----------|
| Net income for the year | 26,928 | 56,253 | 22,712 | 26,928 |
| Earnings per share (in NIS) (*) | 3.16 | 6.61 | 2.67 | |
| Number of shares used in computation (*) | 8,513,473 | 8,513,473 | 8,513,473 | 8,513,473 |

(1) See Note 2A(1).

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

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

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

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

| | Share capital | Capital reserves | Translation adjustments relating to foreign held autonomous Subsidiary | Retained earnings |
|---|---------------|------------------|--|-------------------|
| Balance - January 1, 2002 (Adjusted Amounts (3)) | 28,788 | 156,799 | - | 181,272 |
| Changes during 2002: | | | | |
| Dividend declared after balance-sheet date | | | | (32,843) |
| Net income for the year | | | | 22,712 |
| Balance - December 31, 2002 (Adjusted Amounts (3)) | 28,788 | 156,799 | - | 171,141 |
| Changes during 2003: | | | | |
| Dividend paid | | | | |
| Net income for the year | | | | 56,253 |
| Balance - December 31, 2003 (Adjusted Amounts (3)) | 28,788 | 156,799 | - | 227,394 |
| Changes during 2004: | | | | |

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| | | | | |
|--|--------|---------|---------|----------|
| Distribution of bonus shares | 250 | 23,615 | | (23,865) |
| Translation adjustments relating to foreign held autonomous Subsidiary (2) | | | (3,377) | |
| Net income for the year | | | | 26,928 |
| Balance - December 31, 2004 (Reported Amounts (1)) | 29,038 | 180,414 | (3,377) | 230,457 |

(1) See Note 2A(1).

(2) See Note 2B.

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

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

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

| | Consolidated | | | |
|---|-------------------------|----------------------|----------------------|----------------------|
| | Year ended December 31, | | | |
| | 2 0 0 4 | 2 0 0 3 | 2 0 0 2 | 2 0 0 1 |
| | Reported Amounts (1) | Adjusted Amounts (3) | Adjusted Amounts (3) | Reported Amounts (1) |
| Cash flows - operating activities | | | | |
| Net income | 26,928 | 56,253 | 22,712 | 26,928 |
| Adjustments to reconcile net income to net cash provided by operating activities (Appendix A) | 30,683 | 4,190 | 14,324 | 60,443 |
| Net cash provided by operating activities | 57,611 | 60,443 | 37,036 | 87,371 |
| Cash flows - investing activities | | | | |
| Withdrawal of short-term bank deposit | - | - | 57,069 | - |
| Withdrawal of long-term bank deposits | 8,138 | 9,195 | 8,759 | 8,138 |
| Acquisition of fixed assets | (25,191) | (26,953) | (76,523) | (17,000) |
| Proceeds from sale of fixed assets | 1,827 | 1,092 | 456 | 1,827 |
| Net cash used in investing activities | (15,226) | (16,666) | (10,239) | (8,035) |
| Cash flows - financing activities | | | | |
| Dividend paid | - | (32,843) | (43,790) | - |
| Long-term loans received | 57,672 | 28,949 | 11,386 | 57,672 |

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| | | | | |
|--|----------|----------|----------|----------|
| Repayment of long-term loans | (15,162) | (24,960) | - | |
| Short-term bank credit | (1,087) | 1,087 | - | (1,087) |
| | ----- | ----- | ----- | ----- |
| Net cash provided by (used in) financing activities | 41,423 | (27,767) | (32,404) | (18,648) |
| | ----- | ----- | ----- | ----- |
| Translation adjustments of cash and cash equivalents of foreign held autonomous Subsidiary (2) | (3,784) | - | - | |
| | ----- | ----- | ----- | ----- |
| Increase (decrease) in cash and cash equivalents | 80,024 | 16,010 | (5,607) | 78,427 |
| Cash and cash equivalents - beginning of year | 37,340 | 21,330 | 26,937 | 31,643 |
| | ----- | ----- | ----- | ----- |
| Cash and cash equivalents - end of year | 117,364 | 37,340 | 21,330 | 109,290 |
| | ===== | ===== | ===== | ===== |

(1) See Note 2A(1).

(2) See Note 2B.

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

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

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

| Consolidated | | | |
|-------------------------|-------------------------|-------------------------|-------------------------|
| Year ended December 31, | | | Year |
| 2 0 0 4 | 2 0 0 3 | 2 0 0 2 | 2 0 0 4 |
| ----- | ----- | ----- | ----- |
| Reported Amounts (1) | Adjusted Amounts (2) | Adjusted Amounts (2) | Reported Amounts (1) |
| ----- | ----- | ----- | ----- |

A. Adjustments to reconcile
net income to net cash provided
by operating activities

Income and expenses items
not involving cash flows:

| | | | | |
|---|-------|-------|-------|---|
| Minority interest in earnings of Subsidiary | 3,098 | 7,135 | 2,599 | - |
| Equity in net losses (earnings) of | | | | |

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| | | | | |
|--|----------|----------|----------|----------|
| Subsidiaries | - | - | - | 16,260 |
| Depreciation and amortization | 23,468 | 25,213 | 22,086 | 14,702 |
| Deferred taxes, net | (5,011) | 8,251 | 1,072 | 8,512 |
| Loss (gain) from sale of fixed assets | (1,162) | (482) | 81 | (205) |
| Effect of exchange rate differences, net | (1,901) | (2,266) | 2,202 | (258) |
| Changes in assets and liabilities: | | | | |
| Decrease (increase) in trade receivables | 15,763 | (47,933) | (14,411) | 1,799 |
| Decrease (increase) in other receivables | (20,938) | (2,115) | 4,860 | (6,211) |
| Increase in inventories | (46,919) | (6,237) | (16,362) | (12,646) |
| Increase in trade payables | 49,624 | 27,544 | 18,343 | 8,392 |
| Net change in balances with related parties | 13,591 | (10,050) | 7,731 | 28,985 |
| Increase (decrease) in other payables and accrued expenses | 1,070 | 5,130 | (13,877) | 1,604 |
| | ----- | ----- | ----- | ----- |
| | 30,683 | 4,190 | 14,324 | 60,934 |
| | ----- | ----- | ----- | ----- |
| B. Non-cash activities | | | | |
| Acquisition of fixed assets on credit | 18,470 | 8,661 | 13,707 | 11,619 |

(1) See Note 2A(1).

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

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - GENERAL

A. Description

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

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

B. Definitions:

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The Company - Hogla-Kimberly Ltd.

The Group - the Company and its Subsidiaries, a list of which is provided in Note 9D.

Subsidiaries - companies in which the Company exercises over 50% ownership and control, directly or indirectly, and whose financial statements are fully consolidated with those of the Company.

Related Parties - as defined by Opinion No. 29 of the Institute of Certified Public Accountants in Israel.

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

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

NIS - New Israeli Shekel.

CPI - the Israeli consumer price index.

Dollar - the U.S. dollar.

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

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

C. Use of Estimates

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

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

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HOGLA-KIMBERLY LTD. NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

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

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of Foreign Operations as described in paragraph B below.

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

(1) Definitions

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

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

(2) General

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

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

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

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

(3) Basis of presentation

a. Balance Sheet Items

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

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December 31, 2003 are presented at their Adjusted Amount.

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

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

(3) Basis of presentation (cont.)

a. Balance Sheet Items (cont.)

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

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

b. Statement of Operations Items

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

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

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

(4) Principles of Adjustment through December 31, 2003

a. Balance Sheet Items

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

Investments in Subsidiaries and minority

interest were determined based on the dollar adjusted financial statements of these companies.

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

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

b. Statement of Operations Items

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

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

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

b. Statement of Operations Items (cont.)

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

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

c. Adjustment and Translation of Foreign Subsidiaries Financial Statements

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

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

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

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

- o All differences resulting from the translation of the foreign entity's financial statements by the method described above, are included in a separate component of shareholders' equity as "Translation adjustments relating to foreign held autonomous Subsidiary".

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

C. Principles of Consolidation

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

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

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

D. Cash and Cash Equivalents

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

E. Allowance for Doubtful Accounts

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

F. Inventories

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

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

other

G. Investments in Subsidiaries

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

H. Fixed Assets

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

where the Company intends to exercise such option, or their useful life.

The annual depreciation and amortization rates are: %

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

Impairment of Long-Lived Assets

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

I. Other Assets - Goodwill

Goodwill derived from the acquisition of Subsidiary in Turkey is amortized based on the straight line method over 15 years (see also C above). Impairment examinations and recognition are performed and determined based on the accounting policy outlined in H above. In March 2004, the Israeli Accounting Standard Board issued Standard No. 20 "The Amortization Period of Goodwill". Standard No. 20 calls for the amortization of goodwill over its useful life, based on a systematic method that should reflect the estimated expected period in which the

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goodwill is to contribute economic benefits. The amortization period shall not exceed 20 years from the date on which the goodwill was initially recognized. Standard No. 20 is in effect for reporting periods commencing January 1, 2004, and its provisions are to be applied on a prospective basis. The implementation of Standard No. 20 did not, and is not expected to, affect the Group's financial position and results of operations.

J. Supplier Discounts

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

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HOGLA-KIMBERLY LTD. NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

K. Deferred Income Taxes

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

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

L. Dividends

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

M. Revenue Recognition

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

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

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

N. Earnings Per Share

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

O. Exchange Rates and Linkage Basis

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

O. Exchange Rates and Linkage Basis (cont.)

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

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

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| | | |
|-------------------|-------|------|
| December 31, 2003 | (7.6) | (15) |
| December 31, 2002 | 7.3 | 13 |

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

P. Reclassification

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

Q. Recent Accounting Standards - Income Taxes

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

NOTE 3 - CASH AND CASH EQUIVALENTS

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 4 - TRADE RECEIVABLES

Consolidated

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

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

NOTE 5 - OTHER RECEIVABLES

| | | Consolidated | | |
|---------------------------|--|--------------------|---------------------|--|
| | | December | | |
| | | 2 0 0 4 | 2 0 0 3 | |
| | | Reported Amount | Adjusted Amounts | |
| | | NIS in thousands | | |
| Deferred taxes (Note 22D) | | 4,611 | 5,518 | |
| Prepaid expenses | | 2,175 | 2,908 | |
| Advances to suppliers | | 615 | 3,074 | |
| Value added taxes | | 15,970 | 236 | |
| Income tax advances, net | | 10,973 | 1,467 | |
| Loans to employees | | 600 | 477 | |
| Other | | 781 | 542 | |
| | | ----- | ----- | |
| | | 35,725 | 14,222 | |
| | | ===== | ===== | |

(*) Reclassified.

NOTE 6 - INVENTORIES

| | | Consolidated | | |
|--|--|--------------|---------|--|
| | | December | | |
| | | 2 0 0 4 | 2 0 0 3 | |

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 7 - LONG-TERM BANK DEPOSITS

| | Interest rate ----- % (*) | Consolidated ----- December | |
|------------------------------|------------------------------------|---|---|
| | | 2 0 0 4 Reported Amounts ----- | 2 0 0 3 Adjusted Amounts ----- |
| | | NIS in thousands | |
| A. Composition | | | |
| Linked to the U.S. dollar | 1.75 | 68,928 | 77,946 |
| Less - current maturities | | - | 7,882 |
| | | ----- | ----- |
| | | 68,928 | 70,064 |

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

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

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

NOTE 8 - CAPITAL NOTE OF SHAREHOLDER

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

NOTE 9 - INVESTMENTS IN SUBSIDIARIES

A. Composition

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

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 9 - INVESTMENTS IN SUBSIDIARIES (cont.)

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

C. Investment in Ovisan

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

D. Consolidated Subsidiaries

The consolidated financial statements as of December 31,

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2004, include the financial statements of the following Subsidiaries:

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

Subsidiaries of Rakefet:

Hogla-Kimberly Marketing Ltd.

("Marketing")

Shikma Ltd. ("Shikma")

Mollet Marketing Ltd. ("Mollet")

H-K Overseas (Holland) B.V.

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

Ovisan Sihhi Bez Sanai ve Ticaret Anonim

Sirketi ("Ovisan")

Hogla-Kimberly Holding Anonim Sirketi

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

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 10 - FIXED ASSETS

| CONSOLIDATED | Buildings (1) | Leasehold improvements | Machinery and equipment | Motor vehicles |
|---|---------------|------------------------|-------------------------|----------------|
| | ----- | ----- | ----- | ----- |
| Cost: | | | NIS in thousands | |
| Balance - January 1, 2004 (Adjusted Amounts) | 54,869 | 9,268 | 384,618 | 19,048 |
| Changes during 2004: | | | | |
| Additions | 1,184 | 111 | 33,679 | 334 |
| Dispositions | - | - | (4,477) | (5,111) |
| Foreign currency translation adjustments | 305 | - | 829 | 71 |

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| | | | | |
|--|--------------------------|-------------------------|---------------------------|--------------------------|
| Balance - December 31, 2004 (Reported Amounts) | ----- 56,358 ----- | ----- 9,379 ----- | ----- 414,649 ----- | ----- 14,342 ----- |
| Accumulated depreciation: Balance - January 1, 2004 (Adjusted Amounts) | 15,385 | 5,097 | 166,491 | 14,983 |
| Changes during 2004: | | | | |
| Additions | 614 | 841 | 15,911 | 1,968 |
| Dispositions | - | - | (3,946) | (4,985) |
| Foreign currency translation adjustments | 112 | - | 519 | 63 |
| Balance - December 31, 2004 (Reported Amounts) | ----- 16,111 ----- | ----- 5,938 ----- | ----- 178,975 ----- | ----- 12,029 ----- |
| Net book value: December 31, 2004 (Reported Amounts) | 40,247 ===== | 3,441 ===== | 235,674 ===== | 2,313 ===== |
| December 31, 2003 (Adjusted Amounts) | 39,484 ===== | 4,171 ===== | 218,127 ===== | 4,065 ===== |
| COMPANY Cost: | | | | |
| Balance - January 1, 2004 (Adjusted Amounts) | 25,209 | 6,112 | 343,089 | 3,159 |
| Changes during 2004: | | | | |
| Additions | 116 | 111 | 29,816 | 334 |
| Dispositions | - | - | (4,125) | (878) |
| Balance - December 31, 2004 (Reported Amounts) | ----- 25,325 ----- | ----- 6,223 ----- | ----- 368,780 ----- | ----- 2,615 ----- |
| Accumulated depreciation: Balance - January 1, 2004 (Adjusted Amounts) | 11,812 | 3,733 | 142,932 | 3,076 |
| Changes during 2004: | | | | |
| Additions | - | 589 | 13,876 | 18 |
| Dispositions | - | - | (3,681) | (878) |
| Balance - December 31, 2004 (Reported Amounts) | ----- 11,812 ----- | ----- 4,322 ----- | ----- 153,127 ----- | ----- 2,216 ----- |
| Net book value: December 31, 2004 (Reported Amounts) | 13,513 ===== | 1,901 ===== | 215,653 ===== | 399 ===== |
| December 31, 2003 (Adjusted Amounts) | 13,397 ===== | 2,379 ===== | 200,157 ===== | 83 ===== |

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 11 - TRADE PAYABLES

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

NOTE 12 - OTHER PAYABLES AND ACCRUED EXPENSES

| | Consolidated | | R A |
|--|---------------------|---------------------|--------|
| | December 31 | | |
| | 2 0 0 4 | 2 0 0 3 | |
| | Reported Amounts | Adjusted Amounts | |
| | NIS in thousands | | |
| Accrued income taxes, net of advances | 10,464 | 8,663 | |
| Accrued payroll and related expenses | 22,195 | 20,531 | 1 |
| Value Added Tax | 2,695 | 4,779 | |
| Advances from customers | 726 | 1,085 | |
| Other | 2,640 | 2,574 | |
| | 38,720 | 37,632 | 1 |
| | ===== | ===== | |

NOTE 13 - LONG-TERM BANK LOANS

| Interest rate | |
|------------------|-----|
| % (*) | 2 0 |

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 14 - SEVERANCE PAY

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

NOTE 15 - COMMITMENTS AND CONTINGENT LIABILITIES

A. Commitments

- (1) The Group is obligated to pay royalties to a shareholder - see Note 23B.
- (2) The Company and its Subsidiaries lease certain of their facilities under operating leases for varying periods with renewal options. Future minimum lease rentals as of December 31, 2004 are as follows:

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

B. Guarantees

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

C. Liens

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

D. Legal proceedings

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 15 - COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

D. Legal proceedings (cont.)

- (2) In February 2004, a former customer filed a lawsuit against the Company. This lawsuit is a part of multi-suppliers lawsuit, filed by the customer and asking for one billion NIS from the Company and each other supplier for alleged damages. The customer asked for discharge from legal fee and the request was denied. Due to the preliminary stage of the

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proceedings, management is unable to estimate the possible outcome of the lawsuit. However, based on the Company's legal counsels, management estimates that the Company has valid arguments to oppose the lawsuit. Therefore, no provision was recorded in the financial statements relating to this matter.

NOTE 16 - SHARE CAPITAL

A. Composition of Share Capital in Nominal NIS

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

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

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

NOTE 17 - NET SALES

| | Conso | |
|--|------------|-----|
| | Year ended | |
| | 2 0 0 4 | 2 0 |
| | % | |
| A. Sales to major customers (as percentage from total net sales) | | |
| Customer A | 9.9 | 8 |
| Customer B | 11.0 | 10 |

NIS in t
Reported Adju

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| | Amounts | Amo |
|---------------------------------------|---------|-------|
| | ----- | ----- |
| B. Sales from commercial operations | 238,989 | 376 |
| C. Foreign sales (principally Turkey) | 108,102 | 106 |
| | ===== | ===== |

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 18 - COST OF SALES

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

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

NOTE 19 - SELLING EXPENSES

| | Consolidated | | | |
|-------------------------------|-------------------------|----------|----------|----------|
| | Year ended December 31, | | | Year |
| | ----- | ----- | ----- | ----- |
| | 2 0 0 4 | 2 0 0 3 | 2 0 0 2 | 2 0 0 4 |
| | ----- | ----- | ----- | ----- |
| | Reported | Adjusted | Adjusted | Reported |
| | Amounts | Amounts | Amounts | Amounts |
| | ----- | ----- | ----- | ----- |
| | NIS in thousands | | | N |
| Salaries and related expenses | 57,003 | 46,887 | 39,656 | - |
| Maintenance and | | | | |

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| | | | | |
|---------------------------------|---------|---------|---------|--------|
| transportation expenses | 42,283 | 26,596 | 24,332 | 7,206 |
| Advertising and sales promotion | 60,114 | 30,371 | 38,591 | 6,373 |
| Commissions to distributors | 5,130 | 4,571 | 2,007 | - |
| Royalties to a shareholder | 20,468 | 15,642 | 12,220 | 1,679 |
| Depreciation | 3,687 | 3,778 | 4,188 | 28 |
| Other | 5,016 | 2,825 | 2,961 | - |
| | ----- | ----- | ----- | ----- |
| | 193,701 | 130,670 | 123,955 | 15,286 |
| | ===== | ===== | ===== | ===== |

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 20 - GENERAL AND ADMINISTRATIVE EXPENSES

| | Consolidated | | | Year ended December 31, 2004 |
|--------------------------------------|-------------------------|------------------|------------------|------------------------------|
| | Year ended December 31, | | | |
| | 2004 | 2003 | 2002 | |
| | Reported Amounts | Adjusted Amounts | Adjusted Amounts | |
| | ----- | ----- | ----- | ----- |
| | NIS in thousands | | | N |
| Salaries and related expenses | 15,837 | 18,283 | 13,481 | 2,387 |
| Administrative and computer services | 10,150 | 6,287 | 6,210 | 1,640 |
| Services provided by Shareholder | 1,188 | 1,161 | 1,161 | 238 |
| Office maintenance | 4,632 | 5,376 | 2,990 | 230 |
| Depreciation | 522 | 718 | 588 | - |
| Goodwill amortization | 2,832 | 2,768 | 2,768 | - |
| Provision for doubtful accounts | 2,144 | 1,562 | 215 | - |
| Other | 3,724 | 2,891 | 2,528 | 490 |
| | ----- | ----- | ----- | ----- |
| | 41,029 | 39,046 | 29,941 | 4,985 |
| | ===== | ===== | ===== | ===== |

NOTE 21 - FINANCING INCOME (EXPENSES), NET

| | Consolidated | | | Year e |
|--|-------------------------|------------------|------------------|--------|
| | Year ended December 31, | | | |
| | 2004 | 2003 | 2002 | |
| | Reported Amounts | Adjusted Amounts | Adjusted Amounts | |
| | ----- | ----- | ----- | ----- |
| | NIS in thousands | | | NIS |

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

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 22 - INCOME TAXES

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

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

During 2002, the Company's program for the establishment of a new facility for manufacturing paper was granted Approved Enterprise status in accordance with the Law for the Encouragement of Capital Investments, 1959, under "alternative benefits" track. The approval

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 22 - INCOME TAXES (cont.)

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

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

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| | | | | | |
|---|---------|---------|--------|---------|---------|
| Reduction in corporate tax rates (E. below) | (1,594) | - | - | (1,573) | - |
| Differences arising from | | | | | |
| basis of measurement (*) | (2,821) | (7,629) | 3,883 | 537 | (1,753) |
| Income taxes for prior years | (1,003) | 1,437 | (744) | (837) | 1,358 |
| Other differences, net | 729 | (618) | 739 | 729 | (419) |
| | ----- | ----- | ----- | ----- | ----- |
| | 10,244 | 20,566 | 19,232 | 17,627 | 11,775 |
| | ===== | ===== | ===== | ===== | ===== |

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

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 22 - INCOME TAXES (cont.)

D. Deferred Taxes

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

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| Consolidated | | Company | |
|---------------------|---------------------|---------------------|---------------------|
| December 31, | | | |
| 2 0 0 4 | 2 0 0 3 | 2 0 0 4 | 2 0 0 3 |
| Reported Amounts | Adjusted Amounts | Reported Amounts | Adjusted Amounts |
| NIS in thousands | | NIS in thousands | |

Deferred taxes are presented in the balance sheets as follows:

| | | | | |
|--|----------|---------|---------|---------|
| Long-term liabilities (in respect of depreciable assets) | 37,388 | 29,428 | 35,013 | 26,738 |
| Other receivables (in respect of temporary differences) - Note 5 | (4,611) | (5,518) | (1,532) | (1,769) |
| Other Assets | (15,108) | - | - | - |
| | 17,669 | 23,910 | 33,481 | 24,969 |

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

E. Reduction of Corporate Tax Rates

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

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

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 23 - RELATED PARTIES AND INTERESTED PARTIES

A. Balances with Related Parties

| Consolidated | | Company | |
|---------------------|---------------------|---------------------|---------------------|
| December 31, | | | |
| 2 0 0 4 | 2 0 0 3 | 2 0 0 4 | 2 0 0 3 |
| Reported Amounts | Adjusted Amounts | Reported Amounts | Adjusted Amounts |

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| | NIS in thousands | | NIS in thousands | |
|------------------------------|------------------|--------|------------------|--------|
| Trade receivables (*) | 1,373 | 554 | 18,731 | 8,354 |
| | ===== | ===== | ===== | ===== |
| Capital note - shareholder | 32,770 | 32,770 | 32,770 | 32,770 |
| | ===== | ===== | ===== | ===== |
| Capital notes - Subsidiaries | - | - | 4,205 | 4,205 |
| | ===== | ===== | ===== | ===== |
| Trade payables (*) | 39,055 | 23,752 | 31,251 | 24,097 |
| | ===== | ===== | ===== | ===== |

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

B. Transactions with Related Parties and Subsidiaries

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

(*) Company - excludes Subsidiaries in Israel.

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

NOTE 24 - DISCLOSURE AND PRESENTATION OF FINANCIAL INSTRUMENTS

A. Credit Risk

The revenues of the Group's principal Subsidiaries are derived

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

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

B. Fair Value of Financial Instruments

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

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

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

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

A. Balance Sheets

| | Com |
|---|---------|
| | Dece |
| | 2 0 0 4 |
| | NIS in |
| Current Assets | |
| Cash and cash equivalents | 109,717 |
| Current maturities of long-term bank deposits | - |
| Trade receivables | 113,448 |
| Other receivables | 12,360 |
| Inventories | 71,185 |
| | ----- |
| | 306,710 |
| Long-Term Investments | |
| Capital note of shareholder | 32,770 |

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| | |
|-------------------------------------|---------|
| Investments in Subsidiaries | 169,303 |
| | ----- |
| | 202,073 |
| Fixed Assets, net | 220,520 |
| | ----- |
| | 729,303 |
| Current Liabilities | |
| Short-term bank credit | - |
| Trade payables | 265,546 |
| Other payables and accrued expenses | 12,249 |
| | ----- |
| | 277,795 |
| | ----- |
| Shareholders' Equity | 451,508 |
| | ----- |
| | 729,303 |
| | ===== |

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

B. Statement of Operations

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

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| | | | |
|---|--------|--------|--------|
| Equity in net earnings of Subsidiaries | 16,660 | 29,682 | 8,881 |
| | ----- | ----- | ----- |
| Net income for the year | 36,642 | 62,615 | 47,297 |
| | ===== | ===== | ===== |

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HOGLA-KIMBERLY LTD.
NOTES TO FINANCIAL STATEMENTS (CONT.)

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

C. Statements of Changes in Shareholders' Equity

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

=====

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EXHIBIT 19(a) (iv)

[GRAPHIC OMITTED]

Kesselman & Kesselman
Certified Public Accountants
Trade Tower, 25 Hamered Street
Tel Aviv 68125 Israel
P.O Box 452 Tel Aviv 61003
Telephone +972-3-7954555
Facsimile +972-3-7954556

Report of Independent Accountants on
Financial Statement Schedule

To the Board of Directors of
American Israeli Paper Mills Limited.

Our audits of the consolidated financial statements referred to in our report dated March 10, 2005, appearing in the 2004 annual report to the shareholders of American Israeli Paper Mills Limited also included an audit of Financial Statement Schedule - Valuation and Qualifying Accounts - listed in Item 18 on this Form 20-F. In our opinion, the Schedule presents fairly, in all material respects, the information set forth therein when read in conjunction with related consolidated financial statements.

Tel-Aviv, Israel
March 10, 2005

/s/ Kesselman & Kesselman
Kesselman & Kesselman
Certified Public Accountants (Isr.)

EXHIBIT 19(a) (v)

[GRAPHIC OMITTED]

|X| Kost Forer Gabbay & Kasierer
3 Aminadav St.
Tel-Aviv 67067, Israel

|X| Phone: 972-3-6232525
Fax: 972-3-5622555

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM
OF ISRAELI GAAP TO U.S. GAAP

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T.M.M. Integrated Recycling Industries Ltd.
Tel Aviv

In connection with our audits of the balance sheets of T.M.M. Integrated Recycling Industries Ltd. ("the Company") as of December 31, 2004 and 2003, and the related statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2004 (not presented separately herein), we have also audited the information in the Reconciliation of Israeli GAAP to U.S. GAAP ("the Reconciliation"). The Reconciliation is the responsibility of the Company's management. Our responsibility is to express an opinion on the Reconciliation based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Reconciliation is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the Reconciliation. An audit also includes assessing the accounting principles used and significant estimates made by the management, as well as evaluating the overall Reconciliation presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the information set forth in the Reconciliation presents fairly, in all material respects, in relation to the financial statements of the Company taken as a whole, the financial position and the operating results of the Company in conformity with accounting principles generally accepted in the United States.

Tel-Aviv, Israel
March 8, 2005

/s/ KOST FORER GABBAY & KASIERER
KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

T.M.M. INTEGRATED RECYCLING INDUSTRIES LTD.

RECONCILIATION OF ISRAELI GAAP TO U.S. GAAP
(In thousands of NIS)

A. Shareholders' equity as of December 31, 2004 as reported in the financial statements of the Company prepared in accordance with accounting principles generally accepted in Israel
Adjustments to conform with accounting principles generally accepted in the United States:
Inflation adjustments (1,25
Capitalized start-up costs, net of tax effect (1,16
Amortization of goodwill 6,23

Adjusted Shareholders' Equity in accordance with accounting principles generally accepted in the United States

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B. Net income for the year ended December 31, 2004 as reported in the financial statements of the Company prepared in accordance with accounting principles generally accepted in Israel

Adjustments to conform with accounting principles generally accepted in the United States:

Inflation adjustments

Reversal of capitalized start-up costs, net of tax effect

Amortization of goodwill

79
(32
2,08

Adjusted net income for the year ended December 31, 2004 in accordance with accounting principles generally accepted in the United States

C. Changes in shareholders' equity for the year ended December 31, 2004 in accordance with accounting principles generally accepted in the United States

Balance as of January 1, 2004

Net income

Balance as of December 31, 2004

T.M.M. INTEGRATED RECYCLING INDUSTRIES LTD.

RECONCILIATION OF ISRAELI GAAP TO U.S. GAAP

(In thousands of NIS)

A. Shareholders' equity as of December 31, 2003 as reported in the financial statements of the Company prepared in accordance with accounting principles generally accepted

in Israel

Adjustments to conform with accounting principles generally accepted in the United States:

Inflation adjustments

Capitalized start-up costs, net of tax effect

Amortization of goodwill

(2,04
(84
4,15

Adjusted Shareholders' Equity in accordance with accounting principles generally accepted in the United States

B. Net loss for the year ended December 31, 2003 as reported in the financial statements of the Company prepared in

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accordance with accounting principles generally accepted
in Israel

Adjustments to conform with accounting principles generally accepted in
the United States:

| | |
|---|-------|
| Inflation adjustments | 2,62 |
| Reversal of capitalized start-up costs, net of tax effect | (11 |
| Amortization of goodwill | 2,08 |
| | ----- |

Adjusted net income for the year ended December 31, 2003
in accordance with accounting principles generally
accepted in the United States

- C. Changes in shareholders' equity for the year ended
December 31, 2003 in accordance with accounting
principles generally accepted in the United States
- | | |
|---------------------------------|--|
| Balance as of January 1, 2003 | |
| Net income | |
| Balance as of December 31, 2003 | |

T.M.M. INTEGRATED RECYCLING INDUSTRIES LTD.

RECONCILIATION OF ISRAELI GAAP TO U.S. GAAP
(In thousands of NIS)

- A. Shareholders' equity as of December 31, 2002 as Reported in the
financial statements of the Company prepared in accordance with
accounting principles generally accepted
in Israel
- Adjustments to conform with accounting principles generally
accepted in the United States:
- | | |
|---|-------|
| Inflation adjustments | (6,32 |
| Capitalized start-up costs, net of tax effect | (72 |
| Amortization of goodwill | 2,07 |
| | ----- |

Adjusted Shareholders' Equity in accordance with accounting
principles generally accepted in the United States

- B. Net income for the year ended December 31, 2002
as Reported in the financial statements of the Company
prepared in accordance with accounting principles
generally accepted in Israel

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Adjustments to conform with accounting principles generally accepted in the United States:

| | |
|---|------|
| Inflation adjustments | 3,53 |
| Reversal of capitalized start-up costs, net of tax effect | (14 |
| Amortization of goodwill | 2,07 |

Adjusted net income for the year ended December 31, 2002
in accordance with accounting principles generally accepted
in the United States

C. Changes in shareholders' equity for the year ended
December 31, 2002 in accordance with accounting principles
generally accepted in the United States

| |
|---------------------------------|
| Balance as of January 1, 2002 |
| Net income |
| Balance as of December 31, 2002 |

[GRAPHIC OMITTED]

Kesselman & Kesselman
Certified Public Accountants
Trade Tower, 25 Hamered Street
Tel Aviv 68125 Israel
P.O Box 452 Tel Aviv 61003
Telephone +972-3-7954555
Facsimile +972-3-7954556

Report of Independent Registered Public Accounting Firm on Reconciliation
of Israeli GAAP to U.S. GAAP

To the Shareholders of
American Israeli Paper Mills Ltd.

In connection with our audits of the consolidated balance sheets of American Israeli Paper Mills Ltd. ("the Company") as of December 31, 2004 and 2003, and the related consolidated statements of income, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2004 (the "Financial Statements"), which are incorporated in this Form 20-F, we have also audited the information included in the Reconciliation of Israeli GAAP to U.S. GAAP listed under Item 18 herein. Those financial statements and the Reconciliation are the responsibility of the Company's Board of directors and management. Our responsibility is to express an opinion on the financial statements and the Reconciliation based on our audit.

We did not audit the U.S.GAAP financial data of certain associated companies in

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which the Company's share in excess of profits over losses of which is a net amount of re-measured NIS 30.8 million in 2004 and re-measured NIS 24.7 million in 2003. The financial data of those companies were audited by other independent auditors whose reports have been furnished to us, and our opinion, insofar as it relates to amounts included for those companies, is based solely on the reports of the other independent auditors.

We conducted our audit in accordance with auditing standards generally accepted in Israel, and the standards of the Public Company Accounting Oversight Board (United States), which include examining, on a test basis, evidence supporting the amounts and disclosures in the attached report, in order to obtain reasonable assurance that there is no material misstatement, and to provide us with a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of the other independent auditors, the information set forth under Item 18 present fairly, in all material respects, in relation to the Financial Statements taken as a whole the financial position and the operating results of the Company in conformity with accounting principles generally accepted in the United States.

Tel-Aviv, Israel
March 10, 2005

/s/ Kesselman & Kesselman
Kesselman & Kesselman
Certified Public Accountants (Isr.)

Date: March 7, 2005
Our ref: 783910

To: Rakefet Marketing and Trade Services Ltd.
Ramla

Gentlemen,

Re: US GAAP Adjustments Report as of December 31, 2004

Pursuant to your request and as the independent accountants of Rakefet Marketing and Trade Services Ltd. ("the Company"), we have audited the Company's US GAAP Adjustments Report as of December 31, 2004 and for the year then ended ("the Report"). The Report, which is enclosed herewith, marked by our Firm's identification seal, is your responsibility.

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

In our opinion, the Report referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004, and the results of operations and changes in shareholders' equity for the year then ended., in accordance with generally accepted accounting principles in the

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United States of America.

Sincerely,

/s/ Brightman Almagor & Co.
Brightman Almagor & Co.
Certified Public Accountants

A Member Firm of Deloitte Touche Tohmatsu

Rakefet Marketing and Trade Services Ltd.

US GAAP Adjustments Report

As of December 31, 2004

As of the date of this letter, the audit of the Company's books has been completed, and the financial statements of the Company are to be prepared in accordance with generally accepted accounting principles ("GAAP") applicable in Israel. The following describes the effects on the Company's financial statements had the Company would have prepared its financial statements in accordance with GAAP applicable in the United States of America.

A. Basis of Measurement - Adjusted NIS vis-a-vis Nominal NIS

According to Israeli GAAP, the financial statements of the Company through December 31, 2003 were presented based on nominal historical cost adjusted for the changes in the exchange rate of the U.S. Dollar in relation to the NIS based on the principles presented in Note 2A(4) to the Mother-Company's (Hogla-Kimberly Ltd.) financial statements as of December 31, 2004, while according to US GAAP, the financial statements are to be presented in nominal historical terms. Accordingly, the effect of the difference in the basis of measurement on the Company's financial position and results of operations is excluded for the U.S. GAAP presentation. As presented in Note 2A to the Mother-Company's financial statements as of December 31, 2004, commencing January 1, 2004, the Company ceased the presentation of its financial statements based on adjusted NIS, and effective with the interim financial statements as of March 31, 2004 and for the reporting periods thereafter, including the year ended December 31, 2004, the Company's financial statements are prepared and presented in Reported Amounts, as defined in Note 2A(1) to the Mother-Company's financial statements as of December 31, 2004.

B. Selected Balance Sheet Items

As of December 31, 2004

| As reported | Adjustment | As per US GAAP |
|------------------|------------|----------------|
| NIS in thousands | | |

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| | | | |
|----------------------|---------|-------|---------|
| Shareholders' equity | 267,695 | 1,797 | 269,492 |
| | ===== | ===== | ===== |

Rakefet Marketing and Trade Services Ltd.

US GAAP Adjustments Report
As of December 31, 2004

C. Selected Statements of Operation Items

| | Company |
|---|-------------------------|
| | Year ended December 31, |
| | 2 0 0 4 |
| | NIS in thousands |
| | ----- |
| Net income under Israeli GAAP | 15,259 |
| Effect of material differences between Israeli GAAP and US GAAP: | |
| Change in basis of measurement | 27 |
| from adjusted NIS to nominal NIS | (61) |
| Deferred taxes | ----- |
| Net income under US GAAP | 15,225 |
| | ===== |

D. Changes in Shareholders' Equity in Accordance with US GAAP

| | NIS in thousands |
|--|------------------|
| | ----- |
| Shareholders' equity under US GAAP as of January 1, 2004 | 254,267 |
| Net income for the year under US GAAP | 15,225 |
| | ----- |
| Shareholders' equity under US GAAP as of December 31, 2004 | 269,492 |
| | ===== |

March 7, 2005

signature

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February 23, 2005

Our ref: 783921

To: Mondi Business Paper Hadera Ltd.
Hadera

Gentlemen,

Re: US GAAP Adjustments Report as of December 31, 2004

Pursuant to your request and as the independent accountants of Mondi Business Paper Hadera Ltd. ("the Company"), we have audited the Company's US GAAP Adjustments Report as of December 31, 2004 and for the year then ended ("the Report"). The Report, which is enclosed herewith, marked by our Firm's identification seal, is your responsibility.

The balance presented in the Report under the "Shareholders' equity under US GAAP as of January 1, 2004" line item was audited by other auditors, who issued their unqualified accountants report in relation thereto in March 18, 2004.

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

In our opinion, the Report referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004, and the results of operations and changes in shareholders' equity for the year then ended, in accordance with generally accepted accounting principles in the United States of America.

Sincerely,

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

Mondi Business Paper Hadera Ltd.

US GAAP Adjustments Report
As of December 31, 2004

The consolidated financial statements of the Company have been prepared in accordance with generally accepted accounting principles ("GAAP") applicable in Israel. The following describes the effects on the Company's consolidated financial statements had the Company prepared its financial statements in accordance with GAAP applicable in the United States of America.

A. Recent accounting pronouncements by the FASB

- (1) SFAS No. 151 - Inventory Costs, an Amendment of ARB No. 43, Chapter 4 - In November 2004 the FASB issued SFAS No. 151, "Inventory Costs, an Amendment of ARB No. 43, Chapter 4". SFAS No. 151 amends the guidance in ARB 43, Chapter 4, "Inventory Pricing", which provides guidance on the allocation of certain costs to inventory. SFAS 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage) should be recognized as current-period charges. In addition, SFAS 151 requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. The provisions of this statement are effective for inventory costs incurred during fiscal years beginning after June 2005. The provisions of this statement shall be applied prospectively. The Company is currently assessing the impact of the adoption of this Standard on the Company's financial position and results of operations under U.S. GAAP.
- (2) SFAS 153, Exchange of Non-Monetary Assets - In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets an amendment of APB No. 29". This Statement amends Opinion 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. The Statement specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. This Statement is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date this Statement is issued. Retroactive application is not permitted. The Company is assessing the impact of the adoption of this Standard, and currently estimates that its adoption is not expected to have a material effect on the Company's financial position and results of operations.

B. Goodwill

According to Israeli GAAP, goodwill is to be amortized over the expected estimated economic life of the asset acquired, while according to US GAAP (SFAS 142), commencing January 2002 goodwill is no longer amortized but rather is reviewed annually (or more frequently if impairment indicators arise) for impairment. Following are the corresponding balance-sheet items presented according to US GAAP with regard to the goodwill associated with the acquisition of Miterani (see Note 7B to the Company's financial statements as of December 31, 2004) and the other GAAP differences outlined in D. Below.

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Mondi Business Paper Hadera Ltd.

US GAAP Adjustments Report
As of December 31, 2004

C. Basis of Measurement - Adjusted NIS vis-a-vis Nominal NIS

According to Israeli GAAP, the financial statements of the Group through December 31, 2003 were presented based on nominal historical cost adjusted for the changes in the exchange rate of the U.S. Dollar in relation to the NIS based on the principles presented in Note 2A(4) to the Company's financial statements as of December 31, 2004, while according to US GAAP, the financial statements are to be presented in nominal historical terms. Accordingly, the effect of the difference in the basis of measurement on the Group's financial position and results of operations is excluded for the U.S. GAAP presentation. As presented in Note 2A to the Company's financial statements as of December 31, 2004, commencing January 1, 2004, the Group ceased the presentation of its financial statements based adjusted NIS, and effective with the interim financial statements as of March 31, 2004 and for the reporting periods thereafter, including the year ended December 31, 2004, the Group's financial statements are prepared and presented in Reported Amounts, as defined in Note 2A(1) to the Company's financial statements as of December 31, 2004.

D. Selected Balance Sheet Items

| | As of December 31, 2004 | | |
|-------------------------|-------------------------|------------|-------------------|
| | As reported | Adjustment | As per US GAAP |
| | NIS in thousands | | |
| | ----- | ----- | ----- |
| Other assets - Goodwill | 3,800 | 1,678 | 5,478 |
| | ===== | ===== | ===== |
| Shareholders' equity | 99,187 | (2,313) | 96,874 |
| | ===== | ===== | ===== |

Mondi Business Paper Hadera Ltd.

US GAAP Adjustments Report
As of December 31, 2004

E. Selected Statements of Operation Items

Consolidated and Company

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 Year ended December 31,

 2 0 0 4

 NIS in thousands

| | |
|---|---------|
| Net income under Israeli GAAP | 17,262 |
| Effect of material differences between Israeli GAAP and US GAAP: | |
| Change in basis of measurement from adjusted NIS to nominal NIS | (1,104) |
| Amortization of goodwill | 623 |
| Deferred taxes | 440 |
| | ----- |
| Net income under US GAAP | 17,221 |
| | ===== |

F. Changes in Shareholders' Equity in Accordance with US GAAP

| | |
|--|------------------|
| | NIS in thousands |
| | ----- |
| Shareholders' equity under US GAAP as of January 1, 2004 | 79,653 |
| Net income for the year under US GAAP | 17,221 |
| | ----- |
| Shareholders' equity under US GAAP as of December 31, 2004 | 96,874 |
| | ===== |

/s/ Avi Magid

Avi Magid
 Chief Financial Officer

March 7, 2005
 Our ref: 783908

To: Hogla-Kimberly Ltd.
 Ramla

Gentlemen,

Re: US GAAP Adjustments Report as of December 31, 2004

Pursuant to your request and as the independent accountants of Hogla-Kimberly Ltd. ("the Company"), we have audited the Company's US GAAP Adjustments Report as of December 31, 2004 and for the year then ended ("the Report"). The Report, which is enclosed herewith, marked by our Firm's identification seal, is your responsibility.

We conducted our audit in accordance with standards of the Public Company Accounting Oversight Board (United States) and with generally accepted auditing standards in Israel, including those prescribed by the Israeli Auditors'

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

In our opinion, the Report referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004, and the results of operations and changes in shareholders' equity for the year then ended, in accordance with generally accepted accounting principles in the United States of America.

Sincerely,

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

Hogla-Kimberly Ltd.

US GAAP Adjustments Report
As of December 31, 2004

The consolidated financial statements of the Company have been prepared in accordance with generally accepted accounting principles ("GAAP") applicable in Israel. The following describes the effects on the Company's consolidated financial statements had the Company prepared its financial statements in accordance with GAAP applicable in the United States of America.

A. Recent accounting pronouncements by the FASB

- (1) SFAS No. 151 - Inventory Costs, an Amendment of ARB No. 43, Chapter 4 - In November 2004 the FASB issued SFAS No. 151, "Inventory Costs, an Amendment of ARB No. 43, Chapter 4". SFAS No. 151 amends the guidance in ARB 43, Chapter 4, "Inventory Pricing", which provides guidance on the allocation of certain costs to inventory. SFAS 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage) should be recognized as current-period charges. In addition, SFAS 151 requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. The provisions of this statement are effective for inventory costs incurred during fiscal years beginning after June 2005. The provisions of this statement shall be applied prospectively. The Company is currently assessing the impact of the adoption of this Standard on the Company's financial position and results of operations under U.S. GAAP.

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- (2) SFAS 153, Exchange of Non-Monetary Assets - In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets an amendment of APB No. 29". This Statement amends Opinion 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. The Statement specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. This Statement is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date this Statement is issued. Retroactive application is not permitted. The Company is assessing the impact of the adoption of this Standard, and currently estimates that its adoption in not expected to have a material effect on the Company's financial position and results of operations.

B. Goodwill

According to Israeli GAAP, goodwill is to be amortized over the expected estimated economic life of the asset acquired, while according to US GAAP (SFAS 142), commencing January 2002 goodwill is no longer amortized but rather is reviewed annually (or more frequently if impairment indicators arise) for impairment. Following are the corresponding balance-sheet items presented according to US GAAP with regard to the goodwill associated with the acquisition of Ovisan (see Note 9B to the Company's financial statements as of December 31, 2004) and the other GAAP differences outlined in D. Below.

Hogla-Kimberly Ltd.

US GAAP Adjustments Report
As of December 31, 2004

C. Basis of Measurement - Adjusted NIS vis-a-vis Nominal NIS

According to Israeli GAAP, the financial statements of the Group through December 31, 2003 were presented based on nominal historical cost adjusted for the changes in the exchange rate of the U.S. Dollar in relation to the NIS based on the principles presented in Note 2A(4) to the Company's financial statements as of December 31, 2004, while according to US GAAP, the financial statements are to be presented in nominal historical terms. Accordingly, the effect of the difference in the basis of measurement on the Group's financial position and results of operations is excluded for the U.S. GAAP presentation. As presented in Note 2A to the Company's financial statements as of December 31, 2004, commencing January 1, 2004, the Group ceased the presentation of its financial statements based adjusted NIS, and effective with the interim financial statements as of March 31, 2004 and for the reporting periods thereafter, including the year ended December 31, 2004, the Group's financial statements are prepared and presented in Reported Amounts, as defined in Note 2A(1) to the Company's financial statements as of December 31, 2004.

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D. Selected Balance Sheet Items

| | As of December 31, 2004 | | |
|-------------------------|-------------------------|------------|-------------------|
| | As reported | Adjustment | As per US GAAP |
| | NIS in thousands | | |
| Other assets - Goodwill | 25,878 | 8,731 | 34,609 |
| Shareholders' equity | 436,532 | (419) | 436,113 |

Hogla-Kimberly Ltd.

US GAAP Adjustments Report
As of December 31, 2004

E. Selected Statements of Operation Items

| | Consolidated and Year ended Decem 2 0 0 4 NIS in thous |
|---|---|
| Net income under Israeli GAAP | 26,928 |
| Effect of material differences between Israeli GAAP and US GAAP: | |
| Change in basis of measurement from adjusted NIS to nominal NIS | 1,254 |
| Amortization of goodwill | 2,832 |
| Deferred taxes | (2,298) |
| Net income under US GAAP | 28,716 |

F. Changes in Shareholders' Equity in Accordance with US GAAP

| | NIS in thous |
|--|--------------|
| Shareholders' equity under US GAAP as of January 1, 2004 | 409,978 |

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| | |
|--|---------|
| Translation adjustments | (2,581 |
| Net income for the year under US GAAP | 28,716 |
| | ----- |
| Shareholders' equity under US GAAP as of December 31, 2004 | 436,113 |
| | ===== |

signature