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א.ג.נ.,

הנדון : **אלביט מערכות בע"מ ("החברה") – דוחות כספיים לרבעון ראשון של שנת 2006**

מצ"ב הדוחות הכספיים ודו"ח ההנהלה על תוצאות פעילות החברה ברבעון הראשון של שנת 2006.

בכוונתנו להגיש דוחות אלה לרשות ניירות ערך בארה"ב.

בכבוד רב,

אילן פכולדר
מזכיר החברה

ELBIT SYSTEMS LTD. AND ITS SUBSIDIARIES

CONDENSED INTERIM CONSOLIDATED
FINANCIAL STATEMENTS

AS OF MARCH 31, 2006

(Unaudited)

(In thousands of U.S. dollars)

ELBIT SYSTEMS LTD. AND ITS SUBSIDIARIES

C O N T E N T S

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ELBIT SYSTEMS LTD. AND ITS SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

U. S. dollars (In thousands)

	March 31, 2006 (Unaudited)	December 31, 2005 (Audited)
CURRENT ASSETS:		
Cash and cash equivalents	$ 87,569	$ 93,887
Short-term bank deposits	454	742
Trading securities	2,236	2,282
Trade receivables, (net of allowance for doubtful accounts in the amount of $3,038 and $3,221 as of March 31, 2006 and December 31, 2005, respectively)	344,106	346,689
Other receivables and prepaid expenses	75,218	67,096
Inventories, net of advances	350,493	328,428
Total current assets	860,076	839,124
INVESTMENTS AND LONG-TERM RECEIVABLES:		
Investments in affiliated companies and a partnership	197,496	194,994
Investments in other companies	6,345	6,345
Compensation receivable in respect of fire damages, net	15,530	15,530
Long-term bank deposits and trade receivables	5,581	2,457
Severance pay fund	135,716	133,570
	360,668	352,896
PROPERTY, PLANT AND EQUIPMENT, NET	285,979	284,997
INTANGIBLE ASSETS:		
Goodwill	63,957	63,957
Other intangible assets, net	76,701	78,771
	140,658	142,728
	$ 1,647,381	$ 1,619,745

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

ELBIT SYSTEMS LTD. AND ITS SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

U. S. dollars (In thousands)

	March 31, 2006 (Unaudited)	December 31, 2005 (Audited)
CURRENT LIABILITIES:		
Short-term bank credit and loans	$ 25,300	$ 30,296
Current maturities of long-term loans	6,862	7,355
Trade payable	140,278	120,260
Dividend payable	5,818	-
Other payables and accrued expenses	227,521	216,539
Customers advances and amounts in excess of costs incurred on contracts in progress	273,072	237,718
Total current liabilities	678,851	612,168
LONG-TERM LIABILITIES:		
Long-term loans	161,296	224,982
Advances from customers	140,341	122,263
Deferred income taxes	30,324	31,424
Accrued termination liability	164,936	165,224
	496,897	543,893
MINORITY INTERESTS	13,570	12,907
SHAREHOLDERS' EQUITY:		
Share capital		
Ordinary shares of New Israeli Shekels (NIS) 1 par value; Authorized – 80,000,000 shares as of March 31, 2006 and December 31, 2005; Issued – 41,451,613 and 41,375,545 shares as of March 31, 2006 and December 31, 2005 respectively; Outstanding – 41,042,692 and 40,966,624 shares as of March 31, 2006 and December 31, 2005, respectively	11,653	11,636
Additional paid-in capital	279,039	278,679
Accumulated other comprehensive loss	(3,081)	(1,340)
Retained earnings	174,773	166,123
Treasury shares - 408,921 shares as of March 31, 2006 and December 31, 2005	(4,321)	(4,321)
	458,063	450,777
	$ 1,647,381	$ 1,619,745

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

ELBIT SYSTEMS LTD. AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

U. S. dollars (In thousands, except share and per share data)

	Three months ended March 31,		Year ended December 31,
	2006	2005	2005
	(Unaudited)		(Audited)
Revenues	$ 334,370	$ 230,688	$ 1,069,876
Cost of revenues	246,830	169,126	786,616
Restructuring expenses	-	-	3,488
Gross profit	87,540	61,562	279,772
Research and development costs, net	21,438	15,166	71,903
Marketing and selling expenses	26,248	16,646	78,648
General and administrative expenses	19,007	12,772	54,417
In process research and development write-off	-	-	7,490
	66,693	44,584	212,458
Operating income	20,487	16,978	67,314
Financial expenses, net	(4,241)	(1,732)	(11,472)
Other income (expenses), net	908	169	(5,326)
Income before taxes on income	17,514	15,415	50,516
Taxes on income	4,604	3,987	16,335
	12,910	11,428	34,181
Equity in net earnings of affiliated companies and partnership	2,267	*1,042	(1,636)
Minority interests in losses (earnings) of subsidiaries	(709)	220	(58)
Net income	$ 14,468	*$ 12,690	$ 32,487
Earnings per share			
Basic net earnings per share	$ 0.35	*$ 0.31	$ 0.80
Diluted net earnings per share	$ 0.35	*$ 0.30	$ 0.78
Number of shares used in computation of basic net earnings per share	41,010	40,645	40,750
Number of shares used in computation of diluted net earnings per share	41,736	41,617	41,623

* Restated see Note 1B.

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

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

U. S. dollars (In thousands, except share and per share data)

	Number of outstanding shares	Share capital	Additional paid-in capital	Accumulated other comprehensive loss	Retained earnings	Treasury shares	Total shareholders' equity	Total comprehensive income
Balance as of January 1, 2005 (Audited)	40,561,026	$ 11,548	$ 274,432	$ (4,742)	$ 155,267	$ (4,321)	$ 432,184	
Exercise of options	405,598	88	3,423	-	-	-	3,511	
Tax benefit in respect of options exercised	-	-	652	-	-	-	652	
Stock based compensation	-	-	172	-	-	-	172	
Dividends paid	-	-	-	-	(21,631)	-	(21,631)	
Other comprehensive income (loss) net of tax:								
Unrealized gains on derivative instruments	-	-	-	6,412	-	-	6,412	6,412
Foreign currency translation differences	-	-	-	(924)	-	-	(924)	(924)
Minimum pension liability adjustment	-	-	-	(2,086)	-	-	(2,086)	(2,086)
Net income	-	-	-	-	32,487	-	32,487	32,487
Total comprehensive income								$ 35,889
Balance as of December 31, 2005 (Audited)	40,966,624	$ 11,636	$ 278,679	$ (1,340)	$ 166,123	$ (4,321)	$ 450,777	
Exercise of options	76,068	17	438	-	-	-	455	
Tax benefit in respect of options exercised	-	-	(78)	-	-	-	(78)	
Dividends declared	-	-	-	-	(5,818)	-	(5,818)	
Other comprehensive income (loss), net of tax:								
Unrealized losses on derivative instruments	-	-	-	(1,788)	-	-	(1,788)	(1,788)
Foreign currency translation differences	-	-	-	77	-	-	77	77
Minimum pension liability adjustment	-	-	-	(30)	-	-	(30)	(30)
Net income	-	-	-	-	14,468	-	14,468	14,468
Total comprehensive income								$ 12,727
Balance as of March 31, 2006 (Unaudited)	41,042,692	$ 11,653	$ 279,039	$ (3,081)	$ 174,773	$ (4,321)	$ 458,063	

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

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (CONT.)

U. S. dollars (In thousands, except share and per share data)

	Number of outstanding shares	Share capital	Additional paid-in capital	Accumulated other comprehensive income (loss)	Retained earnings	Treasury shares	Total shareholders' equity	Total other comprehensive income
Balance as of January 1, 2005 (Audited)	40,561,126	$ 11,548	$ 274,432	$ (4,742)	$ 155,267	$ (4,321)	$ 432,184	
Exercise of options	121,816	28	1,047	-	-	-	1,075	
Tax benefit in respect of options exercised	-	-	287	-		-	287	
Stock-based compensation	-	-	-	212	-	-	212	212
Dividends paid	-	-	-		(5,296)	-	(5,296)	
Unrealized gains on derivative instruments				(425)			(425)	(425)
Foreign currency translation differences	-	-	-	(175)	-	-	(175)	(175)
Net income	-	-	-	-	12,690	-	12,690	12,690
Total comprehensive income								$12,302
Balance as of March 31, 2005 (Unaudited) (*)	40,682,942	$ 11,576	$ 275,766	$ (5,130)	$ 162,661	$ (4,321)	$ 440,552	

* Restated see Note 1B.

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

ELBIT SYSTEMS LTD. AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

U. S. dollars (In thousands)

	Three months ended March 31, 2006	Three months ended March 31, **2005	Year ended December 31, 2005
	(Unaudited)		(Audited)
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$ 14,468	$ 12,690	$ 32,487
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	14,649	10,794	57,718
Purchased in process R&D	-	-	7,490
Stock based compensation	-	-	172
Deferred income taxes	(1,698)	(527)	6,551
Accrued severance pay, net	(2,464)	(2,114)	(6,707)
Gain on sale of property, plant and equipment	(231)	(250)	(731)
Tax benefit in respect of options exercised	-	287	652
Minority interests in earnings (losses) of subsidiaries	709	(220)	58
Equity in net losses (earnings) of affiliated companies and partnership, net of dividend received (*)	(1,736)	(42)	13,805
Changes in operating assets and liabilities:			
Decrease (increase) in short and long-term receivables and prepaid expenses	(9,806)	5,978	(43,420)
Increase in inventories	(20,933)	(28,778)	(43,679)
Increase (decrease) in trade payable, other payables and accrued expenses	30,251	(21,197)	(37,859)
Increase in advances received from customers	52,300	72,897	202,450
Settlement of royalties with the Office of the Chief Scientist	-	-	(1,371)
Other adjustments	(98)	45	-
Net cash provided by operating activities	75,411	49,563	187,616
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property, plant and equipment	(14,628)	(15,235)	(58,735)
Acquisition of subsidiaries and businesses (Schedule A)	-	(318)	(28,331)
Investments in affiliated companies	-	(9,681)	(160,861)
Proceeds from sale of property, plant and equipment	1,323	829	2,712
Proceeds from sale of investment	-	3,100	3,100
Investment in long-term bank deposits	(215)	(359)	(1,089)
Proceeds from sale of long-term bank deposits	168	535	1,501
Short-term bank deposits, net	334	(525)	(4)
Net cash used in investing activities	(13,018)	(21,654)	(241,707)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from exercise of options	455	1,075	3,511
Repayment of long-term bank loans	(82,031)	(12,613)	(85,035)
Receipt of long-term bank loans	18,353	-	216,500
Dividends paid	-	-	(21,631)
Change in short-term bank credit and loans, net	(5,488)	(871)	524
Net cash provided by (used in) financing activities	(68,711)	(12,409)	113,869
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(6,318)	15,500	59,778
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	93,887	34,109	34,109
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	$ 87,569	$ 49,609	$ 93,887
* Dividend received	$ 500	$ 1,000	$ 12,169

** Restated see Note 1B.

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

CONSOLIDATED STATEMENTS OF CASH FLOW

U. S. dollars (In thousands)

	Three months ended March 31, 2006	Three months ended March 31, 2005	Year ended December 31, 2005
	(Unaudited)	(Unaudited)	(Audited)
SUPPLEMENTARY CASH FLOWS ACTIVITIES:			
Cash paid during the period for:			
Income taxes	$ 4,218	$ 4,818	$ 21,475
Interest	$ 4,930	$ 1,695	$ 13,151

SCHEDULE A:

Subsidiaries and businesses acquired

Estimated net fair value of assets acquired and liabilities at the date of acquisition assumed:

Working capital, net (excluding cash and cash equivalents)	-	$ (3,281)	$ 39,273
Property, plant and equipment	-	-	(28,875)
Other long-term assets	-	-	(74,363)
Goodwill and other intangible assets	-	(1,514)	(53,291)
In process R&D	-	-	(7,490)
Deferred income taxes	-	-	5,404
Long-term liabilities	-	4,477	82,730
Minority interest	-	-	8,281
	-	$ (318)	$ (28,331)

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

U. S. dollars (In thousands)

Note 1 - GENERAL

A. The accompanying financial statements have been prepared in a condensed format as of March 31, 2006, and for the three months then ended in accordance with generally accepted accounting principles in the United States (U.S. GAAP) relating to the preparation of financial statements for interim periods. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States but which are not required for interim reporting purposes, have been condensed or omitted. See Note 4 for the reconciliation from U.S. GAAP to accounting principles generally accepted in Israel (Israeli GAAP).

These statements should be read in conjunction with the Company's annual financial statements and accompanying notes as of December 31, 2005.

The interim financial statements reflect all adjustments, which are, in the opinion of management, necessary for a fair presentation. All such adjustments were of a normal recurring nature. Reclassifications have been made to comparative data in the balance sheet as of December 31, 2005 in order to conform to the current year's presentation.

Operating results for the three months ended March 31, 2006, are not necessarily indicative of the results that may be expected for the year ending December 31, 2006.

B. During 2004, the Company acquired 4.3% of Tadiran's outstanding shares on the Tel Aviv Stock Exchange in consideration for $15,900. In 2004 and in the first quarter of 2005 the investment in Tadiran's shares was accounted for as available-for-sale securities.

In the first and the second quarters of 2005, the Company acquired additional 17% of Tadiran's outstanding shares in consideration for $74,100.

As a result of the acquisition in the second quarter of 2005, the Company was able to exercise significant influence on Tadiran. In accordance with APB 18, "The Equity Method of Accounting for Investments in Common Stock", the Company's interest in Tadiran, which was previously accounted for as available-for-sale securities, was accounted retroactively under the equity method of accounting ("step-by-step acquisition"). Implementing the step-by-step acquisition method resulted in an adjustment of the Company's financial statements for the first quarter of 2005, in which the Company's investment in Tadiran was accounted for as available-for-sale securities.

The following are the effects of the adjustments on the consolidated statement of income:

	Three months ended March 31, 2005		
	As reported	Effect of adjustments	As adjusted
Equity in net earnings of affiliated companies and partnership	$ 1,493	$ (451)	$ 1,042
Net income	13,141	(451)	12,690
Basic net earnings per share	0.32	(0.01)	0.31
Diluted net earnings per share	$ 0.32	$ (0.02)	$ 0.30

U. S. dollars (In thousands)

Note 2 - SIGNIFICANT ACCOUNTING POLICIES

A. The significant accounting policies followed in the preparation of these statements are identical to those applied in preparation of the latest annual financial statements, except for the adoption of FASB Statement No. 123 (revised 2004), "Share-Based Payments" ("Statement 123(R)") as follows:

Through December 31, 2005 the Company adopted the fair value based method of recording stock options for all employee stock option grants consistent with SFAS No. 123, "Accounting for Stock-Based Compensation" (SFAS No. 123"). Effective January 1, 2006, the Company adopted the provisions of Statement 123(R), using the modified prospective method. The adoption of Statement 123(R) had an immaterial effect on the Company's financial position and results of operations.

B. The accompanying financial statements have been prepared in U.S. dollars since the functional currency of the primary economic environment in which the operations of the Group (which includes Elbit Systems Ltd. and its subsidiaries) are conducted is the U.S. dollar.

Note 3 - INVENTORIES, NET OF ADVANCES

	March 31, 2006 (Unaudited)	December 31, 2005 (Audited)
Cost of long-term contracts in progress	$ 323,920	$ 311,800
Raw materials	88,533	84,343
Advances to suppliers and subcontractors	45,733	40,095
	458,186	436,238
Less - Cost incurred on contracts in progress deducted from customer advances	20,299	16,178
	437,887	420,060
Less -Advances received from customers	78,830	84,083
Provision for losses	8,564	7,549
	$ 350,493	$ 328,428

U. S. dollars (In thousands)

Note 4 - RECONCILIATION TO ISRAELI GAAP

As described in Note 1, the Company prepares its financial statements in accordance with U.S. GAAP. See Note 23 to the 2005 annual financial statements for a description of the differences between U.S. GAAP and Israeli GAAP in respect to the Company. The effects of the differences between U.S. GAAP and Israeli GAAP on the Company's financial statements are detailed below.

A. Effect on net income

	Three months ended March 31,		Year ended December 31,
	2006	2005	2005
	(Unaudited)		(Audited)
Net income as reported according to U.S. GAAP	$ 14,468	$ 12,690	$ 32,487
Adjustments to Israeli GAAP	(633)	(1,522)	(9,637)
Net income according to Israeli GAAP	$ 13,835	$ 11,168	$ 22,850

B. Effect on shareholders' equity

	As reported	Adjustments	As per Israeli GAAP
As of March 31, 2006 (Unaudited)			
Shareholders' equity	$ 458,063	$ (19,912)	$ 438,151
As of December 31, 2005 (Audited)			
Shareholders' equity	$ 450,777	$ (19,279)	$ 431,498

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Elbit Systems Ltd.
Management's Report
For The Quarter Ended March 31, 2006

This report should be read together with the unaudited financial statements for the quarter ended March 31, 2006 of Elbit Systems Ltd. ("Elbit Systems" or the "Company"), the Company's audited consolidated financial statements and related notes for the year ended December 31, 2005, the Company's management report for the year ended December 31, 2005 and the Company's Form 20-F for the year ended December 31, 2004, filed by the Company with the U.S. Securities and Exchange Commission and with the Israeli Securities Authority.

Forward looking statements with respect to the Company's business, financial condition and results of operations in this document are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated in such forward looking statements, including, but not limited to, product demand, pricing, market acceptance, changing economic conditions, risks in product and technology development, the effect of the Company's accounting policies as well as certain other risk factors which are detailed from time to time in the Company's SEC filings.

A. Executive Overview

Business Description

Elbit Systems and its subsidiaries (the "Group") operate in the areas of aerospace, land and naval systems, command, control, communications, computers, intelligence, surveillance and reconnaissance ("C^4ISR"), advanced electro-optic and space technologies, EW suites, airborne warning systems, ELINT systems, data links and military communications systems and equipment. The Group also focuses on the upgrading of existing military platforms and developing new technologies for defense and homeland security applications.

The Group provides support services for the platforms it upgrades as well as the systems and products it supplies. In addition, the Group provides a wide range of logistic support services, including operation of pilot training services for the Israeli Air Force on a private financing initiative basis. Several of the Group's companies also provide advanced engineering and manufacturing services to various customers, utilizing their significant manufacturing capabilities. The Group often cooperates with industries in Israel and in various other countries.

The Group tailors and adapts its technologies, integration skills, market knowledge and battle-proven systems to each customer's individual requirements in both existing and new platforms. By upgrading existing platforms with advanced electronic and electro-optic technologies, the Group provides customers with cost-effective solutions, and its customers are able to improve their technological and operational capabilities within limited defense budgets.

The Group operates in a competitive environment for most of its projects, systems and products. Competition is based on product and program performance, price, reputation, reliability, maintenance costs and responsiveness to customer requirements. This includes the ability to respond to rapid changes in technology. In addition, its competitive position sometimes is affected by specific requirements in particular markets.

Financial Highlights

The financial statements of the Company include consolidation of Elisra's financial results, commencing December 1, 2005.

The Company's revenues increased by 44.9% and reached $334.4 million in the first quarter of 2006, as compared to $230.7 million in the first quarter of 2005.

Net earnings in the first quarter of 2006 were $14.5 million and the diluted earnings per share were $0.35, as compared to $12.7 million and $0.30 in the first quarter of 2005.

The Company's backlog increased by 5% and reached $3.52 billion as of March 31, 2006, as compared to $3.35 billion as of December 31, 2005.

The Company's cash flow generated from operations in the quarter ended March 31, 2006 was $75.4 million, as compared to $49.6 million in the quarter ended March 31, 2005.

The Board of Directors declared a dividend of $0.15 per share for the first quarter of 2006.

B. Backlog of Orders

The Company's backlog of orders as of March 31, 2006 reached $3,523 million, of which 73% were for orders outside of Israel. The Company's backlog as of December 31, 2005 was $3,347 million, of which 72% were for orders outside of Israel.

Approximately 62% of the Company's backlog as of March 31, 2006 is scheduled to be performed in the following three quarters of 2006 and during 2007. The majority of the 38% balance is scheduled to be performed in 2008 and 2009.

C. Critical Accounting Policies and Estimates

The Company's significant accounting policies are described in Note 2 to the audited consolidated financial statements for the year ended December 31, 2005. See also the Company's management report for the year ended December 31, 2005.

D. Summary of Financial Results

The following table sets forth the consolidated statements of operations of the Company and its subsidiaries for the three-month periods ended March 31, 2006 and March 31, 2005.

	For the three months ended March 31			
	2006		2005	
	$	%	$	%
	(In thousands of U.S. dollars, except per share data)			
Total revenues	**334,370**	100.0	**230,688**	100.0
Cost of revenues	**246,830**	73.8	**169,126**	73.3
Gross profit	**87,540**	26.2	**61,562**	26.7
Research and Development (R&D) expenses	**28,578**	8.5	**19,900**	8.6
Less – participation	**(7,140)**	(2.1)	**(4,734)**	(2.0)
R&D expenses, net	**21,438**	6.4	**15,166**	6.6
Marketing and selling expenses	**26,248**	7.8	**16,646**	7.2
General and administrative expenses	**19,007**	5.7	**12,772**	5.5
	66,693	19.9	**44,584**	19.3
Operating income	**20,847**	6.2	**16,978**	7.4
Finance expenses, net	**(4,241)**	(1.3)	**(1,732)**	(0.8)
Other income, net	**908**	0.3	**169**	0.1
Income before taxes on income	**17,514**	5.2	**15,415**	6.7
Taxes on income	**4,604**	1.3	**3,987**	1.7
	12,910	3.9	**11,428**	5.0
Minority interest in losses (gains) of subsidiaries	**(709)**	(0.2)	**220**	0.1
Equity in net earnings of affiliated companies and partnership	**2,267**	0.7	**1,042**	0.5
Net earnings	**14,468**	4.3	**12,690**	5.5
Diluted earnings per share	**0.35**		**0.30**	

First Quarter of 2006 Compared with the First Quarter of 2005

Revenues

The Company's consolidated revenues increased by 44.9%, from $230.7 million in the first quarter of 2005 to $334.4 million in the first quarter of 2006. The increase in revenues was partly as a result of consolidating Elisra's reports, starting December 1, 2005.

The following table sets forth the Company's revenue distribution by areas of operation:

	Three-Month Period ended			
	March 31, 2006		March 31, 2005	
	$ millions	%	$ millions	%
Airborne systems	138.6	41.5	101.0	43.8
Land systems	41.8	12.5	26.0	11.2
C^4ISR systems	83.0	24.8	44.0	19.1
Electro-optics	44.1	13.2	43.2	18.7
Other (mainly non-defense engineering and production services)	26.9	8.0	16.5	7.2
Total	334.4	100.0	230.7	100.0

The changes in revenues distribution by areas of operation, other than ordinary quarterly fluctuations, were in the area of C^4ISR systems sales, which increased mainly as a result of the revenues derived from the Watchkeeper project in the first quarter of 2006. The revenues derived from Elisra are included in the Company's various areas of operation. Elisra's EW systems revenues are included in the Airborne systems area of operation.

The following table sets forth the Company's distribution of revenues by geographical regions:

	Three-Month Period ended			
	March 31, 2006		March 31, 2005	
	$ millions	%	$ millions	%
Israel	94.2	28.2	67.2	29.1
United States	111.0	33.2	89.5	38.8
Europe	54.6	16.3	16.2	7.0
Other countries	74.6	22.3	57.8	25.1
Total	334.4	100.0	230.7	100.0

The Company's sales are primarily to governmental entities and prime contractors under government defense programs. Accordingly, the level of the Company's revenues is subject to governmental budgetary constraints.

The changes in revenues by geographic distribution, other than standard quarterly fluctuations, were in the revenues from customers in Europe, which increased from $16.2 million to $54.6 million, due mainly as a result of the revenues derived from the Watchkeeper project in the first quarter of 2006.

Gross Profit

Gross profit in the quarter ended March 31, 2006 was $87.5 million, as compared to $61.6 million in the quarter ended March 31, 2005. The gross profit margin in the first quarter of 2006 was 26.2%, as compared to 26.7% in the first quarter of 2005.

Research and Development ("R&D")

The Company continually invests in R&D in order to maintain and further advance its technologies, in accordance with a long-term plan, based on its estimate of future market needs.

The Company's R&D included programs which are coordinated with, and partially funded by, third parties, including the Israeli Ministry of Defense ("IMOD"), the Office of the Chief Scientist ("OCS") and bi-national and European Development funds. The R&D was performed in all major areas of core technological activities of the Company and mainly in the areas of advanced airborne systems, cutting edge electro-optics technology and products for surveillance, aerial reconnaissance, lasers, space based sensors and homeland security technologies and products. The Company experienced increased IMOD and OCS participation in these programs.

Gross R&D expenses in the quarter ended March 31, 2006 totaled $28.6 million (8.5% of revenues), as compared to $19.9 million (8.6% of revenues) in the quarter ended March 31, 2005.

The increase in R&D expenses resulted mainly from the consolidation of Elisra's results and projects initiated during 2005, which involved a high level of R&D activities and corresponding third party participations.

Net R&D expenses (after reduction of third party participation) in the quarter ended March 31, 2006 totaled $21.4 million (6.4% of revenues), as compared to $15.2 million (6.6% of revenues) in the quarter ended March 31, 2005.

Marketing and Selling Expenses

The Company maintains its activities in developing new markets and pursues at any given time various business opportunities according to the Company's plan.

Marketing and selling expenses in the quarter ended March 31, 2006 were $26.2 million (7.8% of revenues), as compared to $16.6 million (7.2% of revenues) in the quarter ended March 31, 2005.

The increase in marketing and expenses was mainly as a result of consolidating Elisra's reports starting December 1, 2005.

General and Administrative ("G&A") Expenses

G&A expenses were $19.0 million (5.7% of revenues) in the quarter ended March 31, 2006, as compared to $12.8 million (5.5% of revenues) in the quarter ended March 31, 2005.

The increase in G&A expenses was mainly as a result of consolidating Elisra's reports starting December 1, 2005.

Finance Expense (Net)

Net finance expense in the quarter ended March 31, 2006 was $4.2 million, as compared to $1.7 million in the quarter ended March 31, 2005.

The increase in the net finance expense resulted mainly from a higher level of long-term loans and an increase in interest rates.

Taxes on Income

Provision for taxes in the quarter ended March 31, 2006 was $4.6 million (effective tax rate of 26.3%), as compared to a provision for taxes of $4.0 million (effective tax rate of 25.9%) in the quarter ended March 31, 2005.

The Company's tax rate represents a weighted average of the tax rates to which the various companies in the Group are subject. The change in the effective tax rate is attributable mainly to the mix of the tax rates in the various tax jurisdictions in which the Group's companies generating the taxable income operate.

Company's Share in Earnings of Affiliated Entities

In the first quarter of 2006 the Company had net income of $2.3 million from its share in earnings of affiliated companies and partnerships, as compared to $1.0 million in the first quarter of 2005.

The companies and partnerships, in which the Company holds 50% or less in shares or voting rights and are therefore not consolidated in its financial statements, operate in complementary areas to the Company's core business activities, including electro-optics, airborne systems and communications.

Net Earnings and Earnings Per Share ("EPS")

Net earnings in the quarter ended March 31, 2006 were $14.5 million (4.3% of revenues), as compared to net earnings of $12.7 million (5.5% of revenues) in the quarter ended March 31, 2005. Diluted EPS in the quarter ended March 31, 2006 was $0.35, as compared to $0.30 in the quarter ended March 31, 2005.

The number of shares used for computation of diluted EPS in the quarter ended March 31, 2006 was 41,736 thousand shares, as compared to 41,617 thousand shares in the quarter ended March 31, 2005.

E. Liquidity and Capital Resources

The Company's net cash flow generated from operating activities in the quarter ended March 31, 2006 was $75.4 million, resulting mainly from net income and advances received from customers. The cash inflows were partially offset, mainly by an increase in inventories.

Net cash flow used for investment activities in the quarter ended March 31, 2006 was $13.0 million, which was used mainly for procurement of various assets and equipment.

Net cash flow used for financing activities in the quarter ended March 31, 2006 was $68.7 million, which was used mainly for repayment of long-term loans.

On March 31, 2006, the Company had total borrowings in the amount of $193.5 million, including $161.3 million in long-term loans, and $688.6 million in guarantees issued on its behalf by banks, mainly in respect of advance payment and performance guarantees provided in the regular course of business. On March 31, 2006, the Company had a cash balance amounting to $87.6 million.

As of March 31, 2006, the Company had working capital of $179.0 million and its current ratio was 1.26.

F. Derivatives and Hedges

Market risks relating to the Company's operations result primarily from changes in interest rates and exchange rates. The Company typically uses financial instruments to limit its exposure to those changes. The Company also typically enters into forward contracts in connection with transactions that are denominated in currencies other than U.S. dollars and New Israeli Shekels ("NIS"). The Company may enter from time to time into forward contracts related to NIS, based on market conditions.

On March 31, 2006, the Company's liquid assets were comprised of bank deposits, and it had no investments in liquid equity securities that were subject to market fluctuations, except for its shareholdings in Tadiran Communications Ltd. The Company's deposits and loans are based on variable interest rates, and their value as of March 31, 2006 was therefore not exposed to changes in interest rates. Should interest rates either increase or decrease, such change may affect the Company's results of operations due to changes in the cost of the liabilities and the return on the assets that are based on variable rates.

The Company's functional currency is the U.S. dollar. On March 31, 2006, the Company had exposure due to liabilities denominated in NIS of $60 million in excess of its NIS denominated assets. These liabilities represent mostly wages and trade payables. The amount of the Company's exposure to the changes in the NIS-U.S. dollar exchange rate varies from time to time.

Most of the Company's assets and liabilities which are denominated in currencies other than the NIS and the U.S. dollar were covered as of March 31, 2006 by forward contracts. On March 31, 2006, the Company had forward contracts for the sale and purchase of such foreign currencies totaling $289 million ($93 million in Euro, $191 million in GBP and $5 million in other currencies). The financial derivative activities in the first quarter of 2006 resulted in an unrealized net gain of approximately $3.2 million, which was recorded as other comprehensive income.

On March 31, 2006, the Company had options for hedging future cash flow denominated in NIS in the amount of $14 million. The fair market value of the options as of March 31, 2006 was not material.

G. Dividends

The Board of Directors declared on May 15, 2006 a dividend of $0.15 per share.

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