

DELTA GALIL INDUSTRIES LTD  
Form 20-F/A  
April 13, 2006

AS FILED WITH THE SECURITIES AND EXCHANGE COMMISSION ON APRIL 13, 2006

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SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 20-F/A  
AMENDMENT No. 1

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2004

COMMISSION FILE NUMBER 0-30020

DELTA GALIL INDUSTRIES LTD.  
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

ISRAEL  
(JURISDICTION OF INCORPORATION OR ORGANIZATION)

2 Kaufman Street, Tel Aviv 68012, Israel  
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)

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

NONE  
(Title of each class)

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

ORDINARY SHARES (1)  
(Title of Class)

AMERICAN DEPOSITARY SHARES (2)  
(Title of Class)

- 
- (1) Not for trading, but only in connection with the listing of the American Depositary Shares.
  - (2) Evidenced by American Depositary Receipts, each American Depositary Share representing one ordinary share, par value NIS 1.00 per share.

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 at the close of the period covered by the  
annual report:

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AS OF DECEMBER 31, 2004 THE REGISTRANT HAD 19,947,849 ORDINARY SHARES OUTSTANDING (INCLUDING 1,206,802 ORDINARY SHARES OWNED BY THE REGISTRANT AND 45,882 ORDINARY SHARES HELD BY A TRUSTEE IN CONNECTION WITH THE REGISTRANT'S STOCK OPTION PLANS).

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 elected to follow:

Item 17  Item 18

### EXPLANATORY NOTE

Delta Galil Industries Ltd. is filing this amendment on Form 20-F/A to its Form 20-F ("Original Form 20-F") for the year ended December 31, 2004, originally filed on June 27, 2005, to correct an error contained in the statement of cash flows for the year ended December 31, 2004.

The error relates to the classification of a cash payment of \$4.8 million in fiscal 2004, relating to restructuring expenses recorded as part of the acquisition of Auburn Hosiery Mills. The Company had incorrectly classified the payment as a cash flow used in investing activities rather than cash flows used in operating activities. The following table reflects the adjustments to the statement of cash flows to correct this classification error:

|  | AS REPORTED | CORRECTION      | AS RESTATED |
|--|-------------|-----------------|-------------|
|  | -----       | -----           | -----       |
|  |             | In \$ thousands |             |
| Cash flows from operating activities                 | \$ 27,174   | \$ (4,800)      | \$ 22,374   |
| Cash flows from investing activities                 | (73,689)    | 4,800           | (68,889)    |
| Cash flows from financing activities                 | 50,836      | -               | 50,836      |
| Translation differences on cash and cash equivalents | 130         | -               | 130         |
|  | -----       | -----           | -----       |
| Net increase in cash and cash equivalents            | \$ 4,451    | -               | \$ 4,451    |
|  | =====       | =====           | =====       |

No other financial statement items were affected by the correction of the classification error.

Furthermore, the Company is amending the Original Form 20-F for the following Items:

- a) Amend Item 15 within the Original Form 20-F to clarify the opinion of our Chief Executive Officer and of our Chief

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- Financial Officer with respect to the effectiveness of our internal controls over financial reporting as of December 31 2004. We hereby replace Item 15 of the Original Form 20-F with the amended Item 15 included in this Amendment No. 1;
- b) Include a revised report of Kesselman & Kesselman dated April 11, 2006, on the Consolidated Financial Statements of Delta Galil Industries Ltd., which includes a new note 16 relating to events that occurred after December 31, 2004;
  - c) Include a report of Baker Tilly dated April 10, 2006;
  - d) Include the revised report of Allied for Accounting & Auditing, Member Firm of Ernst & Young Global, dated 30 March, 2006, that refers to the standards of the Public Company Accounting Oversight Board (United States); and
  - e) Amend Item 5 - Operating and Financial Review and Prospects to reflect the restatement to the Consolidated Statement of Cash Flows for the year ended December 31, 2004.

Except as otherwise expressly stated herein and to reflect the changes referred to above, this amended annual report on Form 20-F/A speaks as of the filing date of the Original Form 20-F, and does not purport to reflect events or developments subsequent to the original filing date of the Original Form 20-F.

### PART I

#### ITEM 5: OPERATING AND FINANCIAL REVIEW AND PROSPECTS

THE FOLLOWING DISCUSSION AND ANALYSIS SHOULD BE READ IN CONJUNCTION WITH DELTA GALIL'S CONSOLIDATED FINANCIAL STATEMENTS AND THE NOTES TO THOSE FINANCIAL STATEMENTS INCLUDED IN ITEM 18 OF THIS ANNUAL REPORT. DELTA GALIL'S CONSOLIDATED FINANCIAL STATEMENTS ARE PREPARED IN CONFORMITY WITH US GAAP.

#### LIQUIDITY AND CAPITAL RESOURCES

Delta Galil finances its operations mainly from cash flow from operations, supplemented, if needed, by revolving short-term bank loans and long-term bank loans. Delta Galil repays short-term bank loans if the cash flow from operations exceeds the cash needs for operations and investment.

Following is a breakdown of Delta Galil's cash flows for the last three years in US \$ millions:

|  | YEAR ENDED DECEMBER 31 |        |               |
|--|------------------------|--------|---------------|
|  | 2002                   | 2003   | 2004          |
|  |                        |        | (RESTATEMENT) |
| Net cash flow provided by operating activities *.....  | \$26.3                 | \$42.9 | \$22.4        |
| Net cash flow used in investing activities **.....   | (19.7)                 | (18.4) | (68.9)        |
| Net cash flow provided by financing activities (excluding dividends to shareholders and cost of acquisition of treasury shares)..... | 10.5                   | (11.8) | 59.1          |
| Dividends to shareholders.....   | (7.0)                  | (9.5)  | (8.3)         |
| Cost of acquisition of treasury shares.....  | (8.4)                  | -      | -             |
| Translation differences on cash equivalents of foreign currency consolidated subsidiary.....   | -                      | -      | 0.1           |
|  | -----                  | -----  | -----         |

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|  |       |       |       |
|--|-------|-------|-------|
| Increase in cash and cash equivalents..... | \$1.7 | \$3.2 | \$4.4 |
|  | ===== | ===== | ===== |

\* Net cash provided by operating activities has been decreased by \$ 4.8 million due to a correction of an error in classification of payments made in 2004 relating to restructuring expenses recorded as part of the acquisition of Auburn Hosiery Mills (see note 1A3 of the Notes to the Consolidated Financial Statements).

\*\* Net cash used in investing activities has been increased by \$4,800 thousand due to the correction of an error in classification of payments made in the year 2004, relating to restructuring expenses recorded as part of the acquisition of Auburn Hosiery Mills (see note 1A3 of the Notes to the Consolidated Financial Statements).

In 2002, 2003 and 2004 Delta Galil generated excess cash flow from operations of \$26.3 million, \$42.9 million and \$22.4 million respectively. The decrease in net cash flow provided by operating activities from \$42.9 million in 2003 to \$22.4 million in 2004 is mainly attributed to the decrease in net income. The increase in the net cash flow used in investing activities is mainly attributed to the acquisition of Burlen in the fourth quarter of 2004. Net cash flow used in financing activities in 2004 amounted to \$59.1 million while in 2003 the net cash flow provided by financing activities amounted to \$11.8 million. The decrease in cash flow used in financing activities is attributed mainly to the increase in bank debt in connection with the acquisition of Burlen.

PART II

ITEM 15: CONTROLS AND PROCEDURES

DISCLOSURE CONTROLS AND PROCEDURES. Delta Galil's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of its disclosure controls and procedures as of the end of the period covered by this Annual Report. Based upon such evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that Delta Galil had in place, as of the end of the period covered by this Annual Report, effective controls and procedures designed to ensure that information required to be disclosed by Delta Galil in the reports it files or submits under the Securities Exchange Act of 1934, as amended, and the rules thereunder, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

INTERNAL CONTROLS. There have not been any change in Delta Galil's internal control over financial reporting identified in connection with the evaluation described above that occurred during the period covered by this Annual Report that has materially affected or is reasonably likely to affect, Delta Galil's internal control over financial reporting.

PART III

ITEM 17: FINANCIAL STATEMENTS

Not applicable

ITEM 18: FINANCIAL STATEMENTS

The Consolidated Financial Statements and related notes thereto required by this item are contained on pages F-1 through F-54 hereof.

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ITEM 19: EXHIBITS

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| (B)  | EXHIBITS   |      |
| 1.1  | Memorandum of Association, as amended**  |      |
| 1.2  | Articles of Association**  |      |
| 2.1  | Form of Deposit Agreement and ADR*   |      |
| 4.1  | Stock Purchase Agreement dated as of December 8, 2004 by and among<br>Steven Klein, Kristina Nettesheim, and Gary Beggs, as selling<br>shareholders and Delta Galil Industries Ltd. and Delta Galil USA Inc. as<br>Purchaser relating to the acquisition of Burlen Corp. + ***** |      |
| 4.2  | Second Amended and Related Credit and Security Agreement dated as of<br>December 9, 2004 by and among Delta Galil USA Inc., as Borrower; Bank<br>Leumi USA and Bank Hapoalim B.M., as Lenders and Bank Leumi USA, as<br>Agent. *****   |      |
| 4.3  | Agreement for Purchase and Sale of Stock of Auburn Hosiery Mills, Inc.<br>dated October 30, 2003, by and among Delta Galil USA Inc., Delta Galil<br>Industries Ltd., Delta Galil Holland B.V., CGW Holdings, Inc., GCI<br>Spainco, S.L. and Kellwood Company ****                |      |
| 4.4  | Option Plan to 13 employees of Delta Galil and/or its subsidiaries*  |      |
| 4.5  | Option Plan to Arnon Tiberg*   |      |
| 4.6  | Option Plan to 70 employees of Delta Galil and/or its subsidiaries***  |      |
| 4.7  | Delta Galil Industries Ltd. 2002 Share Option Plan*****  |      |
| 4.8  | Form of Indemnification Undertaking*****   |      |
| 8.1  | List of subsidiaries *****   |      |
| 12.1 | Section 302 Certification of Dov Lautman   |      |
| 12.2 | Section 302 Certification of Yossi Hajaj   |      |
| 13.1 | Section 906 Certification of Dov Lautman   |      |
| 13.2 | Section 906 Certification of Yossi Hajaj   |      |

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- 14.1 Consent of Kesselman & Kesselman
- 14.2 Consent of Baker Tilly
- 14.3 Consents of Allied for Accounting & Auditing, Member Firm of Ernst & Young Global

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\* Previously filed as an exhibit to Delta Galil's Registration Statement on Form F-1 (Registration No. 333-10062) filed with the Securities and Exchange Commission on February 26, 1999 and incorporated herein by reference.  
\*\* Previously filed as an exhibit to Delta Galil's Annual Report on Form 20-F (File No. 0-30020) filed with the Securities and Exchange Commission on June 8, 2001 and incorporated herein by reference

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\*\*\* Previously filed as an exhibit to Delta Galil's Registration Statement on Form S-8 (Registration No. 333-12608) filed with the Securities and Exchange Commission on September 26, 2000 and incorporated herein by reference.  
\*\*\*\* Previously filed as an exhibit to Delta Galil's Annual Report on Form 20-F (File No. 0-30020) filed with the Securities and Exchange Commission on June 23, 2004 and incorporated herein by reference.  
\*\*\*\*\* Previously filed as an exhibit to Delta Galil's Registration Statement on Form S-8 (Registration No. 353-102247) filed with the Securities and Exchange Commission on December 30, 2002 and incorporated herein by reference.  
\*\*\*\*\* Previously filed as an exhibit to Delta Galil's Annual Report on Form 20-F (File No. 0-30020) filed with the Securities and Exchange Commission on June 26, 2003 and incorporated herein by reference.  
\*\*\*\*\* Previously filed as an exhibit to Delta Galil's Annual Report on Form 20-F (File No. 0-30020) filed with the Securities and Exchange Commission on June 27, 2005 and incorporated herein by reference.

+Portions of this exhibit have been omitted and have been filed separately with the secretary of the Securities and Exchange Commission pursuant to a confidential treatment request.

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SIGNATURE

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F/A and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

DELTA GALIL INDUSTRIES LTD.

By: Yossi Hajaj

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Name: Yossi Hajaj  
Title: Chief Financial Officer

Date: April 13, 2006

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2004

DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2004

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The amounts are stated in U.S. dollars (\$) in thousands.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders of  
DELTA GALIL INDUSTRIES LTD.

We have audited the consolidated balance sheets of Delta Galil Industries Ltd. (the "Company") and its subsidiaries as of December 31, 2004 and 2003 and the consolidated 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 did not audit the financial statements of certain subsidiaries, whose assets included in consolidation constitute approximately 12% and 18% of total consolidated assets as of December 31, 2004 and 2003, respectively, and whose revenues included in consolidation constitute approximately 0%, 2% and 10% of total consolidated revenues for the years ended December 31, 2004, 2003 and 2002, respectively. The financial statements of those subsidiaries were audited

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by other independent registered public accounting firms, whose reports have been furnished to us, and our Opinion, insofar as it relates to amounts included for those companies, is based on the reports of the other independent registered public accounting firms.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States of America) and with auditing standards generally accepted in Israel, 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 registered public accounting firms provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of the other independent registered public accounting firms, 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, 2004 and 2003, and the consolidated results of their 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 in the United States of America.

As discussed in Note 1A.3 to the consolidated financial statements, the consolidated statement of cash flows for the year ended December 31, 2004 has been restated.

Tel-Aviv, Israel  
April 11, 2006

Kesselman & Kesselman  
Certified Public Accountant (Isr.)  
A member of PricewaterhouseCoopers  
International Limited

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
CONSOLIDATED STATEMENTS OF INCOME  
(U.S. dollars in thousands, except earnings per share)

|   | YEAR ENDED DECEMBER |           |
|---|---------------------|-----------|
|   | 2004                | 2003      |
| NET REVENUES  | \$654,269           | \$580,130 |
| COST OF REVENUES  | 533,036             | 463,863   |
| GROSS PROFIT  | 121,233             | 116,267   |
| SELLING, MARKETING, GENERAL AND ADMINISTRATIVE EXPENSES - net | 98,646              | 82,089    |
| GAIN (LOSS) ON SALE OF ASSETS AND SUBSIDIARY SHARES           | 922                 | 3,645     |
| RESTRUCTURING EXPENSES  | 1,100               | 1,007     |
| OPERATING INCOME  | 22,409              | 36,816    |



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|   |          |          |
|---|----------|----------|
| FINANCIAL EXPENSES - net                                | 6,231    | 5,637    |
| OTHER INCOME - net                                      | 958      | 252      |
|   | -----    | -----    |
| INCOME BEFORE TAXES ON INCOME                           | 17,136   | 31,431   |
| TAXES ON INCOME   | 2,846    | 7,340    |
|   | -----    | -----    |
|   | 14,290   | 24,091   |
| SHARE IN PROFITS (LOSSES) OF ASSOCIATED COMPANIES - net | (237)    | (300)    |
| MINORITY INTERESTS, NET                                 | (1,368)  | (439)    |
|   | -----    | -----    |
| NET INCOME  | \$12,685 | \$23,352 |
|   | =====    | =====    |
| EARNINGS PER SHARE:                                     |          |          |
| Basic   | \$0.69   | \$1.28   |
|   | =====    | =====    |
| Diluted   | \$0.67   | \$1.24   |
|   | =====    | =====    |
| WEIGHTED AVERAGE NUMBER OF SHARES<br>(IN THOUSANDS):    |          |          |
| Basic   | 18,478   | 18,313   |
|   | =====    | =====    |
| Diluted   | 18,834   | 18,763   |
|   | =====    | =====    |

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
CONSOLIDATED BALANCE SHEETS  
(U.S. dollars in thousands)

|   | DECEMBER 31 |          |
|---|-------------|----------|
|   | 2004        | 2003     |
|   | -----       | -----    |
| ASSETS  |             |          |
| CURRENT ASSETS:                                     |             |          |
| Cash and cash equivalents                           | \$22,150    | \$17,699 |
| Accounts receivable:                                |             |          |
| Trade   | 105,129     | 85,723   |
| Other   | 10,627      | 10,662   |
| Inventories   | 183,767     | 142,984  |
| Deferred income taxes                               | 3,675       | 5,464    |
| Other investment , see note 3                       |             | 1,682    |
|   | -----       | -----    |
| Total current assets                                | 325,348     | 264,214  |
|   | -----       | -----    |
| INVESTMENTS AND LONG-TERM RECEIVABLES:              |             |          |
| Associated company                                  | 455         | 661      |
| Funds in respect of employee rights upon retirement | 6,852       | 6,161    |
| Long-term receivables, net of current maturities    | 226         | 419      |
|   | -----       | -----    |

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|  |           |           |
|--|-----------|-----------|
|  | 7,533     | 7,241     |
| PROPERTY, PLANT AND EQUIPMENT,<br>net of accumulated depreciation and amortization | 128,341   | 124,877   |
| GOODWILL   | 57,920    | 54,358    |
| INTANGIBLE ASSET   | 14,778    |           |
| DEFERRED CHARGES, net of accumulated amortization                                  | 577       | 194       |
| Total assets   | \$534,497 | \$450,884 |

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
CONSOLIDATED BALANCE SHEETS  
(U.S. dollars in thousands)

|  | DECEMBER 31 |          |
|--|-------------|----------|
|  | 2004        | 2003     |
| LIABILITIES AND SHAREHOLDERS' EQUITY                                       |             |          |
| CURRENT LIABILITIES:   |             |          |
| Short-term bank credit   | \$55,603    | \$94,560 |
| Current maturities of long-term bank loans and other liability             | 27,942      | 10,436   |
| Accounts payable and accruals:   |             |          |
| Trade  | 80,338      | 54,464   |
| Other  | 34,083      | 48,142   |
| Total current liabilities  | 197,966     | 207,602  |
| LONG-TERM LIABILITIES:   |             |          |
| Bank loans and other liability, net of current maturities                  | 99,437      | 14,709   |
| Liability for employee rights upon retirement                              | 7,408       | 6,732    |
| Deferred income taxes  | 4,894       | 6,300    |
| Total long-term liabilities  | 111,739     | 27,741   |
| COMMITMENTS AND CONTINGENT LIABILITIES, see note 9                         |             |          |
| Total liabilities  | 309,705     | 235,343  |
| MINORITY INTERESTS   | 3,711       | 3,207    |
| SHAREHOLDERS' EQUITY:  |             |          |
| Ordinary shares of NIS 1 par value   |             |          |
| December 31, 2004 and 2003:  |             |          |
| Authorized - 26,000,000 shares;  |             |          |
| Issued - 19,947,849 shares;  |             |          |
| Issued and paid - 19,901,967 shares and 19,860,211 shares,<br>respectively | 21,840      | 21,830   |

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|  |           |           |
|--|-----------|-----------|
| Additional paid-in capital   | 100,749   | 99,735    |
| Retained earnings  | 108,980   | 104,607   |
| Accumulated other comprehensive loss   | (788)     | (2,503)   |
| Treasury shares, at cost (1,206,802 shares and 1,422,486 shares,<br>in December 31, 2004 and 2003, respectively) | (9,700)   | (11,335)  |
| Total shareholders' equity   | 221,081   | 212,334   |
| Total liabilities and shareholders' equity   | \$534,497 | \$450,884 |

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY  
(U.S. dollars in thousands)

|  | SHARE CAPITAL |           | ADDITIONAL | RETAINED | AC |
|--|---------------|-----------|------------|----------|----|
|  | NUMBER OF     | PAR VALUE | PAID-IN    | EARNINGS | CO |
|  | SHARES        |           | CAPITAL    |          | IN |
|  | IN THOUSANDS  |           |            |          |    |
| BALANCE AT JANUARY 1, 2002   | 19,678        | 21,792    | 98,014     | 81,098   |    |
| CHANGES DURING 2002:   |               |           |            |          |    |
| Net income   |               |           |            | 16,626   |    |
| Losses in respect of derivative<br>instruments designated as a<br>cash-flow hedge (net of related<br>taxes of \$363,000) |               |           |            | (808)    |    |
| Differences from translation of<br>foreign currency financial statements   |               |           |            |          |    |
| Additional minimum pension liability<br>adjustment (net of related<br>taxes of \$540,000)                                |               |           |            |          |    |
| Total comprehensive income   |               |           |            |          |    |
| Exercise of employee stock options   | 2             | *         | 16         |          |    |
| Cash dividend (\$0.37 per share)   |               |           |            | (6,976)  |    |
| Cost of acquisition of treasury shares   |               |           |            |          |    |
| BALANCE AT DECEMBER 31, 2002   | 19,680        | \$21,792  | \$98,030   | \$90,748 |    |
| CHANGES DURING 2003:   |               |           |            |          |    |
| Net income   |               |           |            | 23,352   |    |
| Losses in respect of derivative<br>instruments designated as a<br>cash-flow hedge (net of related<br>taxes of \$474,000) |               |           |            |          |    |
| Differences from translation of<br>foreign currency financial statements   |               |           |            |          |    |
| Additional minimum pension liability   |               |           |            |          |    |

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|  |        |          |           |           |
|--|--------|----------|-----------|-----------|
| adjustment (net of related taxes of \$25,000)  |        |          |           |           |
| Total comprehensive income   |        |          |           |           |
| Exercise of employee stock options   | 181    | 38       | 1,387     |           |
| Tax benefit in respect of employee stock options exercised   |        |          | 318       |           |
| Cash dividend (\$0.52 per share)   |        |          |           | (9,493)   |
|  | -----  | -----    | -----     | -----     |
| BALANCE AT DECEMBER 31, 2003   | 19,861 | \$21,830 | \$99,735  | \$104,607 |
| CHANGES DURING 2004:   |        |          |           |           |
| Net income   |        |          |           | 12,685    |
| Gains in respect of derivative instruments designated as a cash-flow hedge (net of related taxes of \$798,000) |        |          |           |           |
| Differences from translation of foreign currency financial statements  |        |          |           |           |
| Additional minimum pension liability adjustment (net of related taxes of \$30,000)                             |        |          |           |           |
| Total comprehensive income   |        |          |           |           |
| Exercise of employee stock options   | 41     | 10       | 321       |           |
| Tax benefit in respect of employee stock options exercised   |        |          | 79        |           |
| Reissuance of treasury shares on acquisition of Burlen (see note 2a)   |        |          | 614       |           |
| Cash dividend (\$0.45 per share)   |        |          |           | (8,312)   |
|  | -----  | -----    | -----     | -----     |
| BALANCE AT DECEMBER 31, 2004   | 19,902 | \$21,840 | \$100,749 | \$108,980 |
|  | =====  | =====    | =====     | =====     |

\* Less than \$1,000.

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(U.S. dollars in thousands)

|   | YEAR ENDED   |
|---|--------------|
|   | 2004         |
|   | (as resated) |
| CASH FLOWS FROM OPERATING ACTIVITIES*:  |              |
| Net income  | \$12,685     |
| Adjustments to reconcile net income to net cash provided by operating activities: |              |
| Income and expenses not involving cash flows:                                     |              |

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|  |           |
|--|-----------|
| Minority interests in profits of subsidiaries - net                                | 1,368     |
| Share in losses (profits) of associated companies, net                             | 237       |
| Amounts carried to deferred charges  | (597)     |
| Depreciation and amortization  | 15,185    |
| Write-down of other investments  |           |
| Deferred income taxes - net  | (279)     |
| Restructuring expenses   | 1,310     |
| Changes in accrued liability for employee rights upon retirement                   | 1,023     |
| Loss (gain) on amounts funded in respect of employee rights upon retirement        | (416)     |
| Capital loss (gain) on sale of property, plant and equipment and subsidiary shares | (922)     |
| Capital gain from realization of other investment                                  | (958)     |
| Erosion of long-term receivables   | (6)       |
| Exchange differences (erosion) of principal of long-term bank loans - net          | (180)     |
|  | -----     |
|  | 15,765    |
|  | -----     |
| Changes in operating assets and liabilities:                                       |           |
| Decrease (increase) in accounts receivable   | 1,798     |
| Increase (decrease) in accounts payable and accruals                               | 12,204*   |
| Increase in inventories  | (20,078)  |
|  | -----     |
|  | (6,076)   |
|  | -----     |
| Net cash provided by operating activities - forward                                | \$22,374* |
|  | -----     |

\* Net cash provided by operating activities has been decreased by \$4,800 thousand due to the correction of classification of payments made in the year 2004 relating to restructuring expenses recorded as payments of Auburn Hosiery Mills (see note 1A3).

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(U.S. dollars in thousands)

|   | YEAR EN       |
|---|---------------|
|   | -----         |
|   | 2004          |
|   | -----         |
|   | (as restated) |
|   | -----         |
| Brought forward   | \$22,374      |
|   | -----         |
| CASH FLOWS FROM INVESTING ACTIVITIES**:                     |               |
| Acquisition of subsidiaries (1)                             | (56,039)      |
| Additional payment allocated to goodwill                    | (6,700)       |
| Purchase of property, plant and equipment                   | (13,484)      |
| Investment grants relating to property, plant and equipment | 1,074         |
| Other investments   | (58)          |

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|  |          |
|--|----------|
| Proceeds from sale of property, plant and equipment  | 4,318    |
| Proceeds from realization of other investment  | 2,640    |
| Proceeds from sale of subsidiary shares  |          |
| Associated company consolidated in previous years (2)  |          |
| Loans granted to employees   | (260)    |
| Collection of employees loans  | 313      |
| Long term loans granted  | (26)     |
| Amounts funded in respect of employee rights upon retirement - net                               | (667)    |
|  | -----    |
| Net cash used in investing activities  | (68,889) |
|  | -----    |
| CASH FLOWS FROM FINANCING ACTIVITIES:  |          |
| Cost of acquisition of treasury shares   |          |
| Long-term bank loans and other long-term liabilities   | 119,000  |
| Decrease in long-term loans and other long-term liabilities                                      | (10,430) |
| Dividend to the Company's shareholders   | (8,312)  |
| Dividend to minority shareholders in a subsidiary  | (863)    |
| Short-term bank credit - net   | (48,890) |
| Proceeds from exercise of options granted to employees and the company's CEO                     | 331      |
|  | -----    |
| Net cash provided by (used in) financing activities  | 50,836   |
|  | -----    |
| TRANSLATION DIFFERENCES ON CASH AND CASH EQUIVALENTS OF FOREIGN CURRENCY CONSOLIDATED SUBSIDIARY |          |
|  | 130      |
|  | -----    |
| NET INCREASE IN CASH AND CASH EQUIVALENTS  | 4,451    |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR   | 17,699   |
|  | -----    |
| CASH AND CASH EQUIVALENTS AT END OF YEAR   | \$22,150 |
|  | =====    |

\* Less than \$1,000.

(1), (2) See next page for details.

\*\* Net cash used in investing activities has been increased by \$4,800 thousand due to the correction of an error in classification of payments made in the year 2004, relating to restructuring expenses recorded as part of the acquisition of Auburn Hosiery Mills (see note 1A3).

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(U.S. dollars in thousands)

YEAR EN

2004

SUPPLEMENTARY DISCLOSURE OF CASH FLOW

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INFORMATION - CASH PAID DURING THE

YEAR FOR:

|              |                  |
|--------------|------------------|
| Interest     | \$4,133<br>===== |
| Income taxes | \$3,169<br>===== |

(1) ACQUISITION OF SUBSIDIARIES, SEE ALSO NOTE 2:

|  |                   |
|--|-------------------|
| Assets and liabilities of the subsidiaries upon acquisition: |                   |
| Working capital (excluding cash and cash equivalents)        | \$29,944          |
| Long-lived assets  | 9,636             |
| Intangible asset   | 14,778            |
| Goodwill arising on acquisition                              | 4,930             |
|  | 59,288            |
| Reissuance of treasury shares                                | 2,249             |
| Amount payable   | 1,000             |
|  | \$56,039<br>===== |

(2) ASSOCIATED COMPANY PREVIOUSLY CONSOLIDATED:

|  |  |
|--|--|
| Assets and liabilities of the subsidiary previously consolidated |  |
| Working capital (excluding cash and cash equivalents)            |  |
| Fixed assets   |  |
| Long-term liabilities  |  |
| Minority interest in subsidiaries                                |  |
| Investments in an associated company                             |  |

SUPPLEMENTARY INFORMATION ON INVESTING ACTIVITIES NOT INVOLVING CASH FLOWS:

In 2004, 2003 and 2002, the net changes in outstanding balances of trade payables in respect of t plant and equipment were an increase (decrease) of \$ 0.1 million, \$(1.1) million and \$ 0.2 millio

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES:

A. GENERAL:

1) Operations

Delta Galil Industries Ltd. (the "Company") is an Israeli corporation which, together with its subsidiaries (the "Group"), is engaged primarily in

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manufacturing and marketing of intimate apparel, in five reportable operating segments - Delta USA, U.S. upper market, Europe, Socks and Delta marketing Israel. As to the Group's segments and principal markets see note 15.

A significant portion of the Group's revenues derives from three principal customers. See note 12a and 15c.

### 2) Accounting principles

The consolidated financial statements are prepared in accordance with generally accepted accounting principles ("GAAP") in the United States of America.

### 3) Statement of cash flows - restatement

These financial statements have been amended to correct an error in the statement of cash flows for the year ended December 31, 2004. The error relates to the classification of a payment of \$4,800 thousand, made in year 2004, relating to restructuring expenses recorded as part of the acquisition of Auburn Hosiery Mills. The Company is amending the Statement of cash flows to reclassify this payment from cash flows used in investing activities to cash flows used in operating activities.

No other items were affected by the error referred to above.

The following reflect the adjustment to the cash flow statement for the year ended December 31, 2004:

|  | AS REPORTED | CORRECTION      |
|--|-------------|-----------------|
|  | -----       | -----           |
|  |             | In \$ thousands |
| Cash flows from operating activities                 | \$ 27,174   | \$ (4,800)      |
| Cash flows from investing activities                 | (73,689)    | 4,800           |
| Cash flows from financing activities                 | 50,836      | -               |
| Translation differences on cash and cash equivalents | 130         | -               |
|  | -----       | -----           |
| Net increase in cash and cash equivalents            | \$ 4,451    | -               |
|  | =====       | =====           |

### 4) Use of estimates in the preparation of financial statements

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



5) Functional currency

The currency of the primary economic environment in which the operations of the Company and most of its subsidiaries are conducted is the U.S. dollar (the "dollar" or "\$").

Since the U.S. dollar is the primary currency in the economic environment in which the Company operates, monetary accounts maintained in currencies other than the dollar are remeasured using the representative foreign exchange rate at the balance sheet date. Operational accounts and non-monetary balance sheet accounts are measured and recorded at the rate in effect at the date of the transaction. The effects of foreign currency remeasurement are recorded as financial income or expenses as appropriate.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

The functional currency of a subsidiary which was acquired in 2003 (see also note 2c) and an associated company is its local currency (EURO and NIS). The financial statements of this subsidiary are included in consolidation based on translation into dollars in accordance with the principles set forth in Statement of Financial Accounting Standard ("FAS") No. 52 issued by the FASB: assets and liabilities are translated at year end exchange rate, while operating results items are translated at average exchange rates during the year. Differences resulting from translation are presented in shareholders' equity, under accumulated other comprehensive income (loss).

B. PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and all of its subsidiaries. In these financial statements, "subsidiaries" are companies controlled to the extent of over 50%, the financial statement of which are consolidated with those of the Company. Significant intercompany balances and transactions were eliminated in consolidation. Profits from intercompany sales, not yet realized outside the Group, have also been eliminated.

C. CASH EQUIVALENTS

The Group considers all highly liquid investments, which composed of short-term bank deposits (up to three months from date of deposit) that are not restricted as to withdrawal or use, to be cash equivalents.

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### D. INVENTORIES

Inventories are valued at the lower of cost or market. Cost is determined as follows:

Raw materials and supplies, packaging which is part of the production line and maintenance materials - on the "moving average" basis. Finished products and products in process - direct cost of materials (on the "moving average" basis), labor and an appropriate portion of indirect manufacturing costs.

### E. INVESTMENTS IN AN ASSOCIATED COMPANY

An "associated company" is a company over which significant influence is exercised, but which is not a consolidated subsidiary. An associated company is accounted for by the equity method.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

### F. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are stated at cost, net of related investment grants in the amount of \$ 49.8 million and \$ 49.2 million at December 31, 2004 and 2003, respectively. Fixed asset leased by the Group under capital lease are classified as the Group's asset and included at the present value of the minimum lease payments as determined in the lease agreement.

Depreciation is computed by the straight-line method on the basis of the estimated useful life of the assets, at the following annual rates:

|                                |                         |
|--------------------------------|-------------------------|
| Buildings and plumbing         | 2%-7%<br>(mainly 4%)    |
| Machinery and equipment        | 7%-25%<br>(mainly 7%)   |
| Vehicles                       | 15%-20%<br>(mainly 15%) |
| Office furniture and equipment | 6%-25%<br>(mainly 7%)   |

Leasehold improvements are amortized by the straight-line method over the lease period, which is shorter than the estimated useful life of the improvements.

### G. GOODWILL

Under FAS 142 "Goodwill and Other Intangible Assets", goodwill is no longer amortized but tested for impairment at least annually. The Company has selected September 30 of each year as the date on which it will perform its annual goodwill impairment

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test. No impairment resulted from the annual review performed in the year ended December 31, 2004, 2003 and 2002.

### H. DEFERRED CHARGES

Deferred charges represent mainly financing charges, which are amortized over the credit period.

Amortization of deferred charges included among "financial expenses, net" were \$ 353 thousands, \$ 250 thousands and \$ 164 thousands, for the years ended December 31, 2004, 2003 and 2002, respectively.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

#### I. IMPAIRMENT IN VALUE OF LONG-LIVED ASSETS

Under FAS 144 "Accounting for the Impairment or Disposal of Long-Lived Assets" ("FAS 144"), the Company reviews long-lived assets, to be held and used, for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. Under FAS 144, if the sum of the expected future cash flows (undiscounted and without interest charges) of the long-lived assets is less than the carrying amount of such assets, an impairment loss would be recognized, and the assets are written down to their estimated fair values.

As for long - lived assets impairment, see note 12e.

#### J. DEFERRED INCOME TAXES

Deferred taxes are determined utilizing the asset and liability method, based on the estimated future tax effect differences between the financial accounting and tax bases of assets and liabilities under the applicable tax laws. Deferred income tax provisions and benefits are based on the changes in the deferred tax assets or tax liabilities from period to period.

As stated in note 11a, a plant of an Israeli subsidiary has been granted "approved enterprise" status and, accordingly, upon distribution of dividends by this subsidiary to the Company, such dividends may be subject to tax. In light of the Group's policy not to cause distribution of dividends, which would result in additional tax liabilities, any dividends received from the abovementioned subsidiary will be distributed to the Company's shareholders. Accordingly, no account has been taken of the additional tax in respect of the above dividends. See note 11a(1) (a).

The Group does not provide for an additional tax liability with respect to the excess of the amount for financial reporting over the tax basis of investments in non-Israeli subsidiaries, as the

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Company does not expect such temporary differences to be reversed in the foreseeable future.

### K. TREASURY SHARES

Treasury shares held by the Company are presented as a reduction of shareholders' equity, at their cost. The FIFO method was used for the costing of the reissuance of treasury shares, and any resulting gains (net of related tax) are credited to additional paid in capital.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

#### L. REVENUE RECOGNITION

Revenues from sales of products and supplies are recognized when an arrangement (usually in the form of purchase order) exists, delivery has occurred and title passed to the customer, the company's price to the customer is fixed or determinable and collectibility is reasonably assured.

Volume discounts due to customers are estimated based on the terms of the agreements with the customers.

A reserve for sales returns is recorded based on historical experience or specific identification of an event necessitating a reserve.

#### M. CONCENTRATION OF CREDIT RISKS - ALLOWANCE FOR DOUBTFUL ACCOUNTS

The Group's cash and cash equivalents as of December 31, 2004 and 2003 were deposited Mainly with major banks in United States of America, United Kingdom, Hungary and Egypt and in 2003 United States of America, Israel, Hungary and Egypt. The Company is of the opinion that the credit risk in respect of these balances is remote.

A large part of the Group's sales is to 3 principal customers (see also note 15c). The balance receivables from these principal customers as of December 31, 2004 and 2003 were \$ 47,982 thousands and \$ 51,297 thousands, respectively (see also note 12a). The Group does not hold any collateral from these customers; however, based on past experience with those customers, the Group does not anticipate any difficulties in collecting the above balances. The balance of the item "accounts receivable - trade" is composed of a large number of customers. An appropriate allowance for doubtful accounts is included in the accounts in respect of specific debts doubtful of collection. The bad debt income (expenses) and allowance charged to expenses, for the years ended December 31, 2004, 2003 and 2002 aggregated \$ 950 thousands, \$ 309 thousands and \$ (3,558) thousands, respectively.

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### N. SHIPPING AND HANDLING COSTS

The Group's shipping and handling costs are included under selling and marketing expenses in the consolidated statements of income. Shipping and handling costs for the years ended December 31, 2004, 2003 and 2002 were approximately \$ 20 million, \$ 17 million and \$ 18 million, respectively.

### O. ADVERTISING COSTS

These costs are expensed as incurred. Advertising costs for the years ended December 31, 2004, 2003 and 2002 were \$ 2.1 million, \$ 1.9 million and \$ 2.5 million, respectively.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

### P. STOCK BASED COMPENSATION

Stock options granted to employees are accounted for under the recognition and measurement principles of APB No. 25, "Accounting for Stock Issued to Employees", and related interpretations. Under APB 25, compensation cost for employee stock option plans is measured using the intrinsic value based method of accounting.

Accordingly, the difference, if any, between the quoted market price of the ordinary shares on the date of grant of the options and the exercise price of such options is amortized by the accelerated amortization method, against income, over the expected service period (up to four years).

FAS 123, "Accounting for Stock-Based Compensation", established a fair value based method of accounting for employee stock options or similar equity instruments, and encourages adoption of such method for stock compensation plans. However, it also allows companies to continue to account for those plans using the accounting treatment prescribed by APB 25. The Company has elected to continue accounting for employee stock option plans under APB 25, and has accordingly complied with the disclosure requirements set forth in FAS 123, as amended by FAS 148, for companies electing to apply APB 25, (see also note 1t).

The following table illustrates the effect on net income and earnings per share assuming the Company has applied the fair value recognition provisions of FAS 123 to its stock-based employee compensation:

| YEAR ENDED DECE |      |
|-----------------|------|
| 2004            | 2003 |

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|  | \$ IN THOUSANDS<br>(EXCEPT PER SHARE) |           |
|--|---------------------------------------|-----------|
|  | -----                                 | -----     |
| Net income, as reported  | \$ 12,685                             | \$ 23,352 |
| Add - stock-based employee compensation<br>expense include in reported net income<br>net of related tax effect       |                                       |           |
| Less - stock-based employee compensation<br>expense determined under fair value method,<br>net of related tax effect | (690)                                 | (1,384)   |
|  | -----                                 | -----     |
| Pro forma net income   | \$11,995                              | \$ 21,968 |
|  | =====                                 | =====     |
| Earnings per share:  |                                       |           |
| Basic - as reported  | \$ 0.69                               | \$ 1.28   |
| Basic - pro forma  | \$ 0.65                               | \$ 1.20   |
| Diluted - as reported  | \$ 0.67                               | \$ 1.24   |
| Diluted - pro forma  | \$ 0.64                               | \$ 1.17   |

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

The fair value of options granted during 2004, 2003 and 2002 was \$452 thousands, \$72 thousands and \$1,700 thousands, respectively. The fair value of each option granted is estimated on the date of grant using the Black & Scholes option-pricing model, with the following weighted average assumptions:

|                          | 2004   | 2003   | 2002   |
|--------------------------|--------|--------|--------|
|                          | -----  | -----  | -----  |
| Dividend yield           | 3.5%   | 5%     | 5%     |
|                          | =====  | =====  | =====  |
| Expected volatility      | 28.00% | 27.33% | 30.94% |
|                          | =====  | =====  | =====  |
| Risk-free interest rate  | 4%     | 1%     | 2%     |
|                          | =====  | =====  | =====  |
| Expected life - in years | 4.25   | 4.25   | 5.58   |
|                          | =====  | =====  | =====  |

Q. EARNINGS PER SHARE

Basic earnings per share are computed by dividing net income by the weighted average number of shares outstanding during the year, net of treasury shares.

Diluted earnings per share are computed by dividing net income by the weighted average number of shares outstanding during the year, net of treasury shares, taking into account the potential

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dilution that could occur upon the exercise of options granted under employee stock option plans, using the treasury stock method.

### R. DERIVATIVES

The Company enters into forward exchange contracts to hedge the cash flows resulting from sales of products, salaries and wages, in currencies other than the functional currency. The Company does not hold derivative financial instruments for trading purposes.

Under FAS 133 "Hedging Activities", all derivatives are recognized on the balance sheet at their fair value. On the date that the Company enters into a derivative contract, it designates the derivative for accounting purposes, as: (1) hedging instrument, or (2) non-hedging instrument.

For derivative financial instruments that are designated and qualify as a cash flow hedge, the effective portions of changes in fair value of the derivative are recorded in other comprehensive income (loss), under "Gains or losses in respect of derivative instruments designated as a cash-flow hedge, net of related tax" and are recognized in the income statement when the hedged item affects earnings. Ineffective portions of changes in the fair value of cash flow hedges are recognized immediately in income among financial expenses. Changes in the fair value of derivatives that do not qualify for hedge accounting are recognized in income among financial expenses. Cash flows from derivatives that qualify as a cash flow hedge are recognized in the statements of cash flows in the same category as that of the hedged item.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

#### S. COMPREHENSIVE INCOME

In addition to net income, other comprehensive income (loss) includes gains or losses in respect of derivative instruments designated as cash-flow hedge, net of related taxes, differences from translation of foreign currency financial statements of a subsidiary and an associated company and additional minimum pension liability adjustments, net of related taxes.

#### T. 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. In March 2005, the SEC issued Staff Accounting Bulletin No. 107 (SAB 107) regarding the SEC's interpretation of FAS 123R.

FAS 123R eliminates the ability to account for employee share-based payment transactions using APB Opinion No. 25 - "Accounting for Stock Issued to Employees", and requires instead that such transactions be accounted for using the grant-date fair value based method. This Statement will be effective for public companies at the beginning of their next fiscal year that begins after June 15, 2005 (first quarter of 2006 for the Company). Early adoption of FAS 123R is encouraged. 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.

The company estimates that there will not be any cumulative effect of adopting FAS 123R, as of its adoption date by the company (1 January 2006), based on the awards outstanding as of December 31, 2005. This estimate does not include the impact of additional awards, which may be granted, or forfeitures, which may occur subsequent to December 31, 2005 and prior to the adoption of FAS 123R.

The Company expects that upon the adoption of FAS 123R, as of January 1, 2006, the Company 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. Compensation expense for outstanding awards for which the requisite service had not been rendered as of the effective date will be recognized over the remaining service period using the compensation cost calculated for pro-forma disclosure purposes under FAS 123.

The company does not expect this statement to have a material effect on the company's financial statements or its result of operations in future periods.

- 2) 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, its results of operations or cash flows.

- 3) FAS 154 Accounting Changes and Error Corrections - a replacement of Accounting Principles Board Opinion ("APB") No. 20 and FASB Statement No. 3.

In June 2005, the Financial Accounting Standards Board issued FAS No. 154, "Accounting Changes and Error Corrections - a replacement of APB Opinion No. 20 and FASB Statement No. 3". This Statement generally requires retrospective application to prior periods' financial statements of changes in accounting principle. Previously, Opinion No. 20 required that most voluntary changes in accounting principle were recognized by including the cumulative effect of changing to the new accounting principle in net income of the period of the change. FAS 154 applies to all voluntary changes in accounting principle. It also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. When a pronouncement includes specific transition provisions, those provisions should be followed. This Statement shall be effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005 (January 1, 2006 for the company). The Company does not expect the adoption of this statement will have a material impact on the Company's results of operations, financial position or cash flows.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

- 4) In December 2004, the FASB issued FAS No. 153, "Exchanges of Non-monetary Assets - An Amendment of APB Opinion No. 29" (FAS 153). FAS 153 amends APB Opinion No. 29, "Accounting for Non-monetary Transactions" (Opinion 29). The amendments made by FAS 153 are based on the principle that exchanges of non-monetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the exception for non-monetary exchanges of similar productive assets and replace it with a general exception for exchanges of non-monetary assets that do not have commercial substance. The provisions in FAS 153

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are effective for non-monetary 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.

### 5) FAS 155

In February 2006, the FASB issued FAS 155, accounting for certain Hybrid Financial Instruments, an amendment of FASB statements No.133 and 140. This statement permits fair value measurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation. This statement is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. Earlier adoption is permitted as of the beginning of an entity's fiscal year, provided that no interim period financial statements have been issued for the financial year. Management is currently evaluating the impact of this statement, if any, on the Company's financial statements or its results of operations.

### 6) FAS 156

In March 2006 the Financial Accounting Standards Board (the "FASB") issued Statement of Financial Reporting No. 156 ("SFAS 156"). This Statement amends FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, with respect to the accounting for separately recognized servicing assets and servicing liabilities, and is effective for financial periods beginning after September 15, 2006. The Company does not currently engage in transfers of financial fixed assets and accordingly does not anticipate that the adoption of this statement will have a material impact on its financial statements.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

##### U. RECLASSIFICATIONS

Certain figures in respect of prior years have been reclassified to conform with the current year presentation.

#### NOTE 2 - ACQUISITIONS AND OTHER TRANSACTIONS ACQUISITIONS:

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The acquisitions described bellow have all been accounted for by the purchase method. The consideration for each acquisition was attributed to net assets on the basis of the fair value of assets acquired and liabilities assumed.

### A. ACQUISITION OF BURLIN INC. (BURLIN) - IN 2004

On December 8, 2004, the Company acquired, through a wholly owned subsidiary all of the shares of Burlin, a privately held U.S. company, which is engaged in the development, production and marketing of ladies' intimate apparel.

The Burlin acquisition is another step in the Company's strategy to increase its intimate apparel category of the mass market by exploiting the synergies between Burlin's operations and the Company's existing activities. This acquisition is expected to strengthen the Company's position in the mass market.

The acquisition price amounted to \$ 59.6 million from which \$ 56.4 million was paid in cash (including \$ 8.2 million paid to a bank for discharge of a loan) and \$ 2.2 million in ordinary shares comprised of 215,684 ordinary shares reissued from treasury shares, based on a price per share of \$ 10.43. Acquisition costs accrued to \$ 1.0 million would be paid in 2005.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

### NOTE 2 - ACQUISITIONS AND OTHER TRANSACTIONS ACQUISITIONS (continued):

In addition, under the agreement the Company may pay additional amount to the selling shareholders, subject to achieving certain revenues and operating profit targets over a period of 3 years, 2005-2007. The additional consideration, will be recorded as additional goodwill.

Other intangible asset acquired, which amounted to \$ 14.8 million, represents customer relations and is amortized over a period of 20 years. The excess of cost of acquisition over the fair value of net assets, on acquisition date - \$ 3.9 million - was allocated to goodwill and included as part of Delta USA segment . Goodwill and customer relations are deductible for tax purposes. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition:

| At December 8, 2004 (in thousands) |         |
|------------------------------------|---------|
| Cash and cash equivalents          | \$2,605 |
| Account receivable - trade         | 20,577  |
| Account receivable - Other         | 117     |
| Inventories                        | 19,677  |
| Intangible asset                   | 14,778  |
| Property, plant, and equipment     | 7,805   |
| Goodwill                           | 3,873   |
|                                    | -----   |

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|                          |          |
|--------------------------|----------|
| Total assets acquired    | \$69,432 |
|                          | =====    |
| Short-term bank credit   | 3,038    |
| Accounts payable - trade | 4,341    |
| Accounts payable - Other | 2,452    |
|                          | -----    |
| Net assets acquired      | \$59,601 |
|                          | =====    |

As to proforma result, see note d below.

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DELTA GALIL INDUSTRIES LTD.  
 (An Israeli corporation)  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - ACQUISITIONS AND OTHER TRANSACTIONS (continued):

B. ACQUISITION OF MANUFACTURING PLANT IN THAILAND (THAILAND) - IN 2004

In December 2004 the Company acquired a manufacturing facility in Thailand for a total consideration of \$2.4 million. From the said amount \$0.9 million was paid for the shares and \$0.8 million to pay off debt to the former shareholders. In addition, the Company assumed bank debt of \$0.7 million. The acquired manufacturing facility in Thailand constitute a "business" under EITF 98-3 - "Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business".

The main strategy for the Thailand plant acquisition is to reduce the sewing cost. The excess of cost of acquisition over the fair value of net assets on acquisition date approximately - \$1.0 million - was allocated to goodwill.

At December 31, 2004 (in thousands)

|                                |         |
|--------------------------------|---------|
| Cash and cash equivalent       | \$61    |
| Account receivable - trade     | 1,025   |
| Account receivable - Other     | 34      |
| Inventories                    | 1,381   |
| Property, plant, and equipment | 1,831   |
| Goodwill                       | 1,057   |
|                                | -----   |
| Total assets acquired          | \$5,389 |
|                                | =====   |
| Short-term bank credit         | 601     |
| Accounts payable - trade       | 528     |
| Accounts payable - Other       | 1,776   |
| Long term debt                 | 131     |
|                                | -----   |
| Net assets acquired            | \$2,353 |
|                                | =====   |

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DELTA GALIL INDUSTRIES LTD.

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(An Israeli corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - ACQUISITIONS AND OTHER TRANSACTIONS (continued):

C. ACQUISITION OF AUBURN HOSIERY MILLS ("AUBURN") - IN 2003

In November 2003, the Company acquired, through wholly owned subsidiaries from Kellwood inc. ("the seller") all of the shares of its two private held U.S. and Irish companies, which are engaged in the operations of design, development, manufacture, sourcing, marketing, distribution and sale of socks. The functional currency of the Irish operation is its local currency - the Euro.

The Group paid \$10.8 million in cash to the seller.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition. The excess of cost of acquisition over the fair value of net assets on acquisition date approximately \$ 1.4 million - was initially allocated to goodwill.

|  |          |
|--|----------|
| At November 13, 2003 (in thousands)    |          |
| Cash and cash equivalents              | \$699    |
| Account receivable - trade             | 5,754    |
| Account receivable - other             | 700      |
| Inventories                            | 9,448    |
| Property, plant, and equipment         | 6,642    |
| Goodwill                               | 1,368*   |
|  | -----    |
| Total assets acquired                  | \$24,611 |
|  | =====    |
| Short-term bank credit                 | \$213    |
| Accounts payable                       | 7,435    |
| Accrued expenses - restructuring costs | 6,163*   |
|  | -----    |
| Net assets acquired                    | \$10,800 |
|  | =====    |

\*In 2003 the Company recorded liabilities in respect of restructuring costs in an amount of \$6.2 million, which includes approximately \$2.2 million for severance pay and related costs and \$ 4.0 million for costs associated with the shut down of certain acquired facilities. An amount of \$4.8 million was paid during 2004, \$2 million related to grants, \$2.3 million related to employees, \$0.1 million related to property, plant and equipment and \$0.4 million related to manufacturing and others.

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DELTA GALIL INDUSTRIES LTD.

(An Israeli corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - ACQUISITIONS AND OTHER TRANSACTIONS (continued):

During 2004 the Company finalized the restructuring plan and

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liabilities in respect of restructuring costs, which results in a decrease of \$1.9 million on the excess of cost of acquisitions over the fair value of net assets on acquisition date. The said decrease was allocated \$ 1.4 million to the goodwill (which offset the entire goodwill initially recognized) and \$ 0.5 million to property, plant and equipment.

- D. Hereafter are certain unaudited pro forma combined income data assuming that the acquisition of Burlen had occurred on January 1, 2004 and 2003, respectively, and the acquisition of Auburn had occurred on January 1, 2003 and 2002, respectively. The unaudited pro forma financial information is not necessarily indicative of the combined results that would have been attained had the acquisitions of Burlen and Auburn occurred as of January 1, 2004 and 2003, and 2003 and 2002, respectively, nor is it necessarily indicative of future results.

|                             | YEAR ENDED DECEMBER 31         |           |           |
|-----------------------------|--------------------------------|-----------|-----------|
|                             | 2004                           | 2003      | 2002      |
|                             | -----<br>IN THOUSANDS<br>----- |           |           |
|                             | (EXCEPT EARNINGS PER SHARE)    |           |           |
|                             | -----<br>(UNAUDITED)<br>-----  |           |           |
| Net Revenues                | \$763,375                      | \$721,172 | \$626,732 |
|                             | =====                          | =====     | =====     |
| Net Income                  | \$19,853                       | \$24,664  | \$16,079  |
|                             | =====                          | =====     | =====     |
| Earning per share - Basic   | \$1.06                         | \$1.33    | \$0.85    |
|                             | =====                          | =====     | =====     |
| Earning per share - Diluted | \$1.04                         | \$1.30    | \$0.85    |
|                             | =====                          | =====     | =====     |

- E. ACQUISITION OF THE OPERATIONS OF KOMAR TEXTILE TRADING CO. LTD. ("KOMAR") - IN 2002

In November 2002 the Company purchased some of the operations of Komar, a privately held Hungarian company. Komar is engaged in production of baby-wear. The purchase price - \$ 5,600 thousands was paid in cash. The excess of cost of acquisition over the fair value of net assets on acquisition date - \$ 753 thousands - was allocated to goodwill, which is included as part of the Europe segment. Goodwill is not deductible for tax purposes. During the fourth quarter of 2004 the group has decided to close the logistic center, and included \$ 1.5 million restructuring expenses, of which \$ 0.4 million is included in cost of revenues. See also note 12e.

- F. ACQUISITION OF INNER SECRETS INC. ("INNER") - IN 2001

In January 2001, the Company acquired, through a wholly owned subsidiary - Wundies Industries Inc. ("the acquiring company"), all of the shares of Inner, a privately held U.S. company, which is engaged in the development, production and marketing of ladies' intimate apparel.

DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - ACQUISITIONS AND OTHER TRANSACTIONS (continued):

The acquisition price was paid as follows: 85% in cash and 15% in Company shares. In addition, the acquisition price was set to be four times Inner's earnings before interest, income taxes, depreciation and amortization ("EBITDA"), subject to certain adjustments, for the year ended December 31, 2000, but after deducting liabilities to banks and other loans as of December 31, 2000.

In addition, in case the EBITDA of both the acquired company and the acquiring company for the year 2002 will be higher than the EBITDA of both companies for the year 2000 by at least \$ 4 million, the sellers will be entitled to an additional cash payment, of an amount not exceeding 50% of the EBITDA of the acquired company for the year 2000 (hereafter - "the performance payment"), in accordance with certain adjustments. In case the sellers' entitlement to full performance payment will not be in accordance with the 2002 results, the sellers will be entitled to receive the rest of the performance payment, in accordance with the agreement, considering the 2003 results. In any case, the sellers will not be entitled to an over-all payment that exceeds the performance payment. Such additional payment will be paid in cash and will be recorded when earned as additional purchase price.

During 2001 the Company paid \$ 48.7 million in cash (including \$ 14.4 million paid to a bank for discharge of a loan) and \$ 5.9 million in 454,020 Company shares, based on a price per share of \$ 13.05. During 2003 and 2004 the Company paid an additional \$ 2.0 million and \$ 6.7 million in cash, respectively, as an adjustment to the purchase price. The payments were allocated to goodwill.

In 2003 the purchase price was finalized and the total goodwill amount, resulted from the acquisition, was \$ 24.3 million, which is included as part of Delta USA segment. Goodwill is not deductible for tax purposes.

OTHER TRANSACTION:

SALE OF SUBSIDIARY'S SHARES

In August 2002, Delta Galil signed an agreement for the sale of 10% of its wholly-owned subsidiary, in consideration of \$250 thousands.

During March 2003 the Company received the payment, transferred the shares and as a result recognized a gain in an amount of \$ 109 thousands.

According to the agreement the buyer has an option to purchase additional shares of the subsidiary on terms to be agreed at a

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later stage. The option shall remain in effect for a period of 36 months from the date of agreement.

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DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 3 - OTHER INVESTMENT AND INVESTMENT IN AN ASSOCIATED COMPANY

A. SALE OF INVESTMENT IN STANDARD TEXTILE EUROPE LTD. ("STE") - OTHER INVESTMENT

On August 4, 2000, a subsidiary signed an agreement for the sale of its investment in STE, which was an associated company (till January 2003), for \$ 9 million, which bears interest of LIBOR plus 1.5% per year.

The transaction was carried out in four equal batches, in the years 2004, 2003, 2002 and 2000. The capital gains recorded in the years 2004, 2003 and 2002 were \$958 thousands, \$885 thousands and \$ 960 thousands, respectively, and were classified to "Other Income - net".

B. EDMIT LTD. ("EDOMIT") - AN ASSOCIATED COMPANY

The Company holds 50% of the shares in Edomit. The Company's investment in Edomit is accounted for by the equity method.

The balance of the investment in Edomit as of December 31, 2004 and 2003 is \$ 455 thousands and \$ 661 thousands, respectively. As of December 31, 2004 and 2003 these balances include a loan in the amount of \$ 446 and \$ 417, respectively. The loan is linked to the Israeli CPI and bears no interest.

NOTE 4 - LONG-TERM RECEIVABLES

Long-term receivables represent long-term loans to employees - mainly linked to the Israeli consumer price index ("CPI") and bearing interest at the rate of 4%.

These balances are mature in the following years after balance sheet dates:

|                                 | DECEMBER 31  |       |
|---------------------------------|--------------|-------|
|                                 | 2004         | 2003  |
|                                 | IN THOUSANDS |       |
| First year - current maturities | \$193        | \$512 |
| Second year                     | 204          | 362   |
| Third year                      | 14           | 36    |
| Fourth year                     | 5            | 21    |
| Fifth year                      | 3            |       |



|       |       |
|-------|-------|
| ----- | ----- |
| \$226 | \$419 |
| ----- | ----- |
| \$419 | \$931 |
| ===== | ===== |

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DELTA GALIL INDUSTRIES LTD..  
 (An Israeli corporation)  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 5 - PROPERTY, PLANT AND EQUIPMENT:

- A. Composition of property, plant and equipment, grouped by major classifications, is as follows:

|  | DECEMBER 31  |           |
|--|--------------|-----------|
|  | 2004         | 2003      |
|  | IN THOUSANDS |           |
|  | -----        | -----     |
| Land, buildings and plumbing, see b. below*                            | \$41,706     | \$33,706  |
| Machinery and equipment  | 134,873      | 122,873   |
| Vehicles, office furniture and equipment<br>and leasehold improvements | 46,729       | 46,729    |
|  | -----        | -----     |
|  | 223,308      | 203,308   |
| Less - accumulated depreciation and amortization                       | (94,967)     | (84,967)  |
|  | -----        | -----     |
|  | \$128,341    | \$118,341 |
|  | =====        | =====     |
| <br>   |              |           |
| * Including building leased under capital lease -<br>(see note 1f):    |              |           |
| Cost   | \$1,414      | \$1,414   |
| Less - accumulated depreciation  | 409          | 409       |
|  | -----        | -----     |
|  | \$1,005      | \$1,005   |
|  | =====        | =====     |

In 2003 the Group recorded a \$3.5 millions capital gain from sale of real estate in London.

B. LAND AND BUILDINGS

Part of the buildings of the Company stand on land leased from the Israel Lands Administration for periods expiring in the years 2016-2037. The leasehold rights have not yet been registered in the Land Registry.

- C. Investment projects of the Company and its subsidiary have been approved by the Israeli Investment Center, under the Law for the Encouragement of Capital Investments, 1959. The balance of

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uncompleted investments as of December 31, 2004 aggregates \$ 6.4 million.

- D. Depreciation and amortization in respect of property, plant and equipment totaled \$ 14.8 , \$14.3 and \$ 13.9 million in the year ended December 31, 2004, 2003 and 2002 (excluding impairment of assets relating to restructuring, see note 12e).
- E. As to pledges on assets, see notes 8d and 11a.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 6 - GOODWILL:

Changes in goodwill during the year:

|  | YEAR ENDED DECEMBER 31, |                    |         |    |
|--|-------------------------|--------------------|---------|----|
|  | IN THOUSANDS            |                    |         |    |
|  | DELTA USA               | US UPPER<br>MARKET | EUROPE  |    |
| Goodwill at beginning of year  | \$ 46,732               | \$2,119            | \$ 753  | \$ |
| Changes during the year:   |                         |                    |         |    |
| Goodwill arising from acquisition of subsidiaries, see notes 2a and 2b | 3,873                   |                    | 1,057   |    |
| Adjustment to purchase price, see note 2c                              |                         |                    |         |    |
| Goodwill at end of year  | \$ 50,605               | \$2,119            | \$1,810 | \$ |

  

|  | YEAR ENDED DECEMBER 31, |                    |        |    |
|--|-------------------------|--------------------|--------|----|
|  | IN THOUSANDS            |                    |        |    |
|  | DELTA USA               | US UPPER<br>MARKET | EUROPE |    |
| Goodwill at beginning of year                                | \$ 40,032               | \$2,119            | \$ 753 | \$ |
| Changes during the year:                                     |                         |                    |        |    |
| Goodwill arising from Acquisition of operations, see note 2c |                         |                    |        |    |
| Adjustment to purchase price, see note 2f                    | 6,700                   |                    |        |    |
| Goodwill at end of year                                      | \$ 46,732               | \$2,119            | \$ 753 | \$ |

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DELTA GALIL INDUSTRIES LTD.  
 (An Israeli corporation)  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 - EMPLOYEE RIGHTS UPON RETIREMENT:

- A. Employee related obligations are composed as follows:  
 B.

|  | DECEMBER 31    |                |
|--|----------------|----------------|
|  | 2004           | 2003           |
|  | IN THOUSANDS   |                |
| Accrued severance pay                          | \$6,076        | \$5,442        |
| Obligation in respect of defined benefit plans | 1,332          | 1,290          |
|  | <u>\$7,408</u> | <u>\$6,732</u> |

As of December 31, 2004 and 2003, the Group had deposits of \$ 5.7 million and \$ 5.1 million, respectively, with funds managed by major Israeli insurance companies, which are earmarked by management to cover the severance pay liability in respect of Israeli employees. Under FAS No. 132, "Employers Disclosures About Pensions and Other Post Retirement Benefits", such deposits are not considered to be "plan assets".

Costs of pension and severance pay charged to income in the years ended December 31, 2004, 2003 and 2002 were \$ 6.9 million, \$ 7.0 million and \$ 6.5 million respectively (in 2004, 2003 and 2002, excluding \$ 190 thousands, \$ 850 thousands and \$ 651 thousands, respectively, relating to the termination of employment, which were charged to restructuring expenses, see note 12e).

The profit (loss) from deposits in respect of severance pay were \$ 416 thousands, \$(214) thousands and \$(624) thousands in the years ended December 31, 2004, 2003 and 2002, respectively.

The main terms of the various arrangements with employees are described in b. below. Further details relating to defined benefit plans, as required by FAS 132, are presented in b and c below.

B. TERMS OF ARRANGEMENTS:

- 1) The Company and Israeli subsidiaries

Israeli law generally requires payment of severance pay and/or pensions upon dismissal of an employee or upon

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termination of employment in certain other circumstances. The following principal plans relate to employee rights upon retirement, as applicable to Israeli companies in the Group:

- a) Pension plans for the majority of the Group's employees - under collective labor agreements, these external pension plans cover the severance pay liability. The pension and severance pay liabilities covered by these plans are not reflected in the financial statements as the pension and severance pay risks have been irrevocably transferred to the pension funds.
- b) Insurance policies for employees in managerial positions - these policies provide coverage for severance pay and pension liabilities of managerial personnel. Under labor agreements these insurance policies are, subject to certain limitations, the property of the employees.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 - EMPLOYEE RIGHTS UPON RETIREMENT (continued):

- c) Severance pay liabilities not covered by the pension funds are fully provided for in these consolidated financial statements, as if it was payable at each balance sheet date on an undiscounted basis, based upon the number of years of service and the most recent monthly salary of the Group's employees in Israel.
- 2) Non-Israeli subsidiary
- A U.S. subsidiary provides various defined benefit pension plans to its employees, see c below.
- At December 31, 2004, the assets of the defined benefit pension plan are primarily invested in group annuity contracts with an insurance company. The plan was frozen effective January 1996.
- Contributions to the defined contribution 401(k) plan are based on a percentage of annual salaries. The Company generally matches 50% of each participant's pretax contribution up to 4% of the participant's annual compensation.

C. CERTAIN DETAILS RELATING TO DEFINED BENEFIT PLANS:

2004

2003

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|  | IN THOUSANDS |         |
|--|--------------|---------|
|  | 2004         | 2003    |
| CHANGE IN BENEFIT OBLIGATION:                  |              |         |
| Benefit obligation at beginning of year        | \$3,145      | \$3,151 |
| Interest cost                                  | 179          | 18      |
| Actuarial loss                                 | 20           |         |
| Benefit paid                                   | (204)        | (19)    |
| Benefit obligation at end of year              | \$3,140      | \$3,140 |
| CHANGE IN PLAN ASSETS:                         |              |         |
| Fair value of plan assets at beginning of year | \$2,888      | \$2,931 |
| Actual return on plan assets                   | 90           | 15      |
| Employer contribution                          | 225          |         |
| Benefit paid, including plan expenses          | (204)        | (19)    |
| Fair value of plan assets at end of year       | \$2,999      | \$2,888 |
| RECONCILIATION OF FUNDED STATUS:               |              |         |
| Funded status (carryforward obligations)       | \$(141)      | \$(25)  |
| Unrecognized net actuarial loss                | 1,332        | 1,291   |
| Adjustment to recognize minimum liability      | (1,332)      | (1,291) |
| Prepaid / pension cost (accrued)               | \$(141)      | \$(25)  |
| WEIGHTED AVERAGE ASSUMPTIONS AT END OF YEAR:   |              |         |
| Discount rate                                  | 5.75%        | 6.00%   |
| Expected return on plan assets                 | 6.25%        | 6.25%   |
| Rate of compensation increase                  | N/A          | N/A     |

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 - EMPLOYEE RIGHTS UPON RETIREMENT (continued):

The consolidated components of net periodic benefits costs are as follows:

|                              | YEAR ENDED DECEMBER 31 |      |
|------------------------------|------------------------|------|
|                              | 2004                   | 2003 |
|                              | IN THOUSANDS           |      |
| Interest cost                | \$179                  | \$18 |
| Actual return on plan assets | (122)                  | (8)  |
| Net amortization             | 10                     | 1    |

-----  
 \$ 67  
 =====

-----  
 \$11  
 =====

D. CASH FLOWS INFORMATION REGARDING THE COMPANY'S LIABILITY FOR EMPLOYEE RIGHTS UPON RETIREMENT:

1. The Company expects to contribute in 2005, \$670 thousands to insurance companies and \$270 thousands to contribution plans.
2. The Company expects to pay the following future benefits to its Israeli employees upon their normal retirement age:

|                 | SEVERANCE PAY<br>BENEFITS |
|-----------------|---------------------------|
| -----           |                           |
| IN THOUSANDS    |                           |
| -----           |                           |
| 2005            | \$52                      |
| 2006            | \$283                     |
| 2007            | \$61                      |
| 2008            | \$801                     |
| 2009            | \$159                     |
| Years 2010-2014 | \$1,196                   |

These amounts, as they relate to the Israeli subsidiaries were determined based on the employees current salary rates and the number of service years that will be accumulated upon their retirement date. These amounts do not include amounts that might be paid to employees that will cease working with the Company before their normal retirement age.

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DELTA GALIL INDUSTRIES LTD.  
 (An Israeli corporation)  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 8 - LONG-TERM LIABILITIES - BANK LOANS AND OTHER LIABILITY:

A. COMPOSITION:

|   | WEIGHTED<br>AVERAGE<br>INTEREST RATE |
|---|--------------------------------------|
| -----                                     |                                      |
| DECEMBER 31,<br>2004                      |                                      |
| -----                                     |                                      |
| %   |                                      |
| Bank loans - in dollars or linked thereto | 3.8%                                 |

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|   |      |
|---|------|
| Bank loans - in Canadian dollars  |      |
| Bank loans - in other currencies  | 5.5% |
| Other liability -   |      |
| Obligation under capital lease, see note 1f<br>and c below - in dollars | 8.6% |
| Less - current maturities   |      |

B. TOTAL LIABILITIES (NET OF CURRENT MATURITIES) MATURE IN THE FOLLOWING YEARS AFTER BALANCE SHEET DATES:

|                           | DECEMBER 31  |          |
|---------------------------|--------------|----------|
|                           | 2004         | 2003     |
|                           | IN THOUSANDS |          |
| Second year               | \$29,703     | \$10,440 |
| Third year                | 23,270       | 1,018    |
| Fourth year               | 23,230       | 1,024    |
| Fifth year                | 22,584       | 1,031    |
| Sixth year and thereafter | 650          | 1,196    |
|                           | \$99,437     | \$14,709 |

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DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 8 - LONG-TERM LIABILITIES - BANK LOANS AND OTHER LIABILITY (continue):

C. A subsidiary of the Company has entered into capital lease agreements for a building it uses; the lease will expire in the year 2014.

Following are the future minimum lease payments, by years, under capital lease and the present value of the net minimum lease payments as of December 31, 2004:

|                                 | IN<br>THOUSANDS |
|---------------------------------|-----------------|
| First year - current maturities | 158             |
| Second year                     | 158             |
| Third year                      | 158             |
| Fourth year                     | 158             |
| Fifth year                      | 158             |
| Sixth year and thereafter       | 790             |

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|                                     |       |
|-------------------------------------|-------|
|                                     | 1,580 |
| Less - amount representing interest | 548   |
|                                     | ----- |
|                                     | 1,032 |
|                                     | ===== |

- D. The balance of liabilities is fully secured by floating charges in an unlimited amount on all the assets and rights of the Company and the assets of its subsidiaries, and/or by fixed charges on the major portion of the Group's fixed assets.
- E. A subsidiary is a party to a credit agreement, which was amended, as of December 9, 2004, with Bank Leumi U.S.A and Bank Hapoalim B.M. Borrowings under the credit agreement are secured by substantially all of the assets of the subsidiary. The credit agreement provides for \$ 130 million in loans, of which \$ 70 million are long term loans which bear interest of Libor +1.4% and the remainder is short term credit which bear interest of Libor +1.15%. The principal of the term loans is payable in 20 equal quarterly installments of approximately \$3.5 million each until December 1, 2009. As of December 31, 2004 the unutilized credit line was \$ 15.2 million.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 9 - COMMITMENTS AND CONTINGENT LIABILITIES:

A. COMMITMENTS

The Company and its subsidiaries lease 30 facilities under operating leases. The leases (including extension options) for 18 facilities expire on various dates between 2006 and 2025 and the remaining leases expired in 2005. The Company intends to renew some of these leases. The minimum future annual lease payment over each of the years 2005 to 2009 will amount to \$7.6, \$6.6, \$6.5, \$6.0 and \$5.4 million, respectively. In the period from 2010 to the end of the lease periods, the cumulative lease payments will amount to \$ 11.2 million. The lease expenses for each of the years 2004, 2003 and 2002 were \$ 8.6 million, \$ 7.3 million and \$ 6.6 million, respectively.

B. CONTINGENT LIABILITIES - GUARANTEES

The Company and its subsidiaries signed a guarantee, each for other, which is unlimited in amount to all of the group's liabilities.

C. As to contingent consideration, see note 2a.

D. The Company entered into agreements that provide the Company rights to market products brand names owned by other parties. Royalties under these agreements are calculated as a percentage of the sales. The royalties rate range from 4% to 16% of sales.



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### NOTE 10 - SHAREHOLDERS' EQUITY:

#### A. SHARE CAPITAL:

- 1) The Company's shares are traded on the Tel-Aviv Stock Exchange ("TASE") and in the form of American Depositary Shares ("ADS's"), each of which represents one ordinary share, on the Nasdaq National Market in the United States. On December 31, 2004, the closing price per ADS on Nasdaq was \$10.34; the shares were quoted on the TASE on that date at NIS 43.81 (\$10.09).
- 2) On December 2004, the Company reissued 215,684 treasury shares as part of the proceeds paid to the selling shareholders of Burlen, see note 2a.
- 3) In December 2002, the Company purchased 565,000 of the Company's shares for an amount of \$ 6,215 thousands (representing \$ 11.0 per share).
- 4) On September 28, 2001, the Company's Board of Directors approved the repurchase of Company shares for an amount of up to \$3.0 million. During 2002 and 2001 the Company purchased 282,483 and 96,017 shares, respectively, in the open market at an average price of \$7.58 and \$9.0 per share in a total amount of \$2,141 thousands and \$860 thousands, respectively.
- 5) As of December 31, 2004 and 2003, the balance of shares issued by the Company for the purpose of future exercise of employee stock options, which is held by a trustee company, is 45,884 and 87,638 shares, respectively.
- 6) The shares held by the Company have no voting rights and are not entitled to receive dividends.

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DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

### NOTE 10 - SHAREHOLDERS' EQUITY (continued):

#### B. STOCK OPTIONS PLANS FOR EMPLOYEES AND THE COMPANY'S CEO:

- 1) On May 10, 1998, the Company's Board of Directors approved an employee stock option plan for the grant, without consideration, of up to 304,696 options, exercisable in purchase of 319,931 ordinary shares of NIS 1 par value of the Company, to thirteen senior employees of the Company and/or its subsidiaries. All of the above options were granted in June 1998. The exercise price of each option is \$ 8.297, based on the quoted price of the Company's shares on the last day of trade prior to the Board of Directors' resolution (\$ 9.22), less 10%. The options vest in four equal batches.

As of December 31, 2004, all the options are fully

vested. The options are exercisable over three years period, commencing on the date that is two years after the date such option vested. Any option not exercised within the said five years will expire. The options expire over the years 2003-2006.

- 2) On September 10, 1998, the Company's Board of Directors approved a plan for the grant, at no consideration, of up to 100,000 options to its CEO, which are exercisable in purchase of 100,000 shares of NIS 1 par value of the Company. All of said options were granted in September 1998. The exercise price of each option is \$ 7.90, based on the quoted price of the Company's share on the last day of trade prior to the Board of Directors' resolution (\$ 8.77), less 10%. The options vest in four equal batches. As of December 31, 2004, all the options are fully vested. The exercise terms under the CEO's plan are identical to those of the employees plan.
- 3) On June 4, 2000, the Company's Board of Directors approved an employee stock option plan for the grant, without consideration, of up to 809,000 options (including 100,000 options to its CEO), exercisable to 809,000 ordinary shares of NIS 1 par value of the Company, to 70 senior employees of the Group ("the optionees"). All the options were granted on August 6, 2000. The exercise price of each option is \$ 21.07, based on the quoted price of the Company's shares on the last day of trade prior to the Board of Directors' resolution.

The options vest in four equal batches: the first, second, third and fourth batch vest in August 2001, 2002, 2003 and 2004, respectively. The options are exercisable over a three years period, commencing one year after the vesting date of each batch.

- 4) On October 23, 2002, the Company's Board of Directors approved an employee stock option plan for the grant, without consideration, of up to 1,100,000 options (including 100,000 options to its CEO), exercisable in purchase of 1,100,000 ordinary shares of NIS 1 par value of the Company. The exercise price of each option is the higher of the quoted price of the Company's shares on the grant day or \$ 9.

On November 22, 2002, the Company granted 1,004,500 options to 97 senior employees of the Group (including 100,000 options to the CEO) at an exercise price of \$ 9. The options vest in four equal batches. The first, second, third and fourth batches will vest in November 2003, 2004, 2005 and 2006, respectively. The options are exercisable over a three-year period, commencing one year after the vesting date of the first batch and on the vesting date of the second, third and fourth batch.

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

### NOTE 10 - SHAREHOLDERS' EQUITY (continued):

In May 2003 the Company granted 30,000 options to three employees of the Group at an exercise price of \$10.76. In March and in August 2004 the Company granted 80,000 and 30,000 options respectively, to six and one employees of the Group, respectively, at an exercise price of \$ 15.35 and \$ 12.74, respectively. The options are exercisable over a three-year period, commencing one year after the vesting date of the first batch and on the vesting date of the second, third and fourth batch.

At December 31, 2004 72,000 options remain available for grant under the plan.

- 5) The grant of options to Israeli employees under the Company's plans is subject to the terms stipulated by Section 102 and 102A of the Israeli Income Tax Ordinance. Inter-alia, that Section provides that the Company will be allowed to claim as an expense for tax purposes the amounts credited to the employees as a benefit, when the related tax is payable by the employee.
- 6) The rights pertaining to the ordinary shares issued upon exercise of the options will be identical to those of the other ordinary shares of the Company.
- 7) Following is a summary of the status of the Company's stock option plans:

|  | YEAR ENDED DECEMBER 31 |  |           |  |
|--|------------------------|--|-----------|--|
|  | 2004                   |  | 2003      |  |
|  | NUMBER*                | WEIGHTED<br>AVERAGE<br>EXERCISE<br>PRICE** | NUMBER*   | WEIGHTED<br>AVERAGE<br>EXERCISE<br>PRICE** |
| Options outstanding at beginning of year | 1,830,702              | \$13.50                                    | 2,038,562 | \$ 13.07                                   |
| Changes during the year:                 |                        |  |           |  |
| Granted - at market price                | 110,000                | \$14.65                                    | 30,000    | \$ 10.76                                   |
| Exercised                                | (41,756)               | \$7.91                                     | (180,109) | \$ 7.91                                    |
| Forfeited                                | (66,875)               | \$9.34                                     | (57,751)  | \$ 11.35                                   |
| Options outstanding at end of year       | 1,832,071              | \$13.84                                    | 1,830,702 | \$ 13.50                                   |
| Options exercisable at end of year       | 1,106,821              | \$14.69                                    | 528,952   | \$ 17.15                                   |

\* Represents the number of shares arising upon exercise of options, based on the conversion ratio.

\*\* Per option.

DELTA GALIL INDUSTRIES LTD.  
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 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 10 - SHAREHOLDERS' EQUITY (continued):

- 8) The following table summarizes information regarding options outstanding at December 31, 2004:

| NUMBER OF SHARES ISSUABLE UPON EXERCISE OF OPTIONS |                              |   |                              |                              |
|--|------------------------------|---|------------------------------|------------------------------|
| EXERCISE PRICES                                    | OUTSTANDING                  |   | VESTED                       | EXERCISABLE                  |
|  | BALANCE AT DECEMBER 31, 2004 | WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE | BALANCE AT DECEMBER 31, 2004 | BALANCE AT DECEMBER 31, 2004 |
|  |                              | YEARS                                       |                              |                              |
| \$8.30   | 65,696                       | 1.2   | 65,696                       | 65,696                       |
| \$7.90   | 50,000                       | 1.4   | 50,000                       | 50,000                       |
| \$21.07  | 688,375                      | 2.0   | 688,375                      | 532,125                      |
| \$9.00   | 888,000                      | 4.4   | 459,000                      | 459,000                      |
| \$10.76  | 30,000                       | 4.8   | 7,500                        |                              |
| \$15.35  | 80,000                       | 5.8   |                              |                              |
| \$12.74  | 30,000                       | 6.1   |                              |                              |
|  | =====                        |   | =====                        | =====                        |
|  | 1,832,071                    |   | 1,270,571                    | 1,106,821                    |
|  | =====                        |   | =====                        | =====                        |

C. RETAINED EARNINGS

In determining the amount of retained earnings available for distribution as a dividend, the Companies Law stipulates that the cost of the Company's shares acquired by the Company (that are presented as a separate item in the statement of changes in shareholders' equity) has to be deducted from the amount of retained earnings.

NOTE 11 - TAXES ON INCOME:

A. THE COMPANY AND CERTAIN ISRAELI SUBSIDIARIES (HEREAFTER - THE COMPANIES):

- 1) Tax benefits under the Israeli Law for the Encouragement of Capital Investments, 1959 ("the law")

The Company and certain Israeli subsidiary have received investment grants from the State of Israel. In the event of failure to comply with the terms attached to the receipt of those grants, the companies may be required to refund the amount of the grants, in whole or in part,

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with linkage differences to the Israeli CPI and interest from the date of receipt.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 11 - TAXES ON INCOME (continued):

The abovementioned companies have registered floating charges on all their assets in favor of the State of Israel as security for compliance with the terms relating to the grants.

Under the law, by virtue of the "approved enterprise" status granted to certain of their enterprises, the Company and its Israeli subsidiary are entitled to various tax benefits, as follows:

a) Reduced tax rates

During the period of benefits - 7 to 10 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) - a reduced tax rate of 25% applies, instead of the regular tax rate, see (4) below. Some of the approved enterprises are eligible for a tax exemption for the first two years commencing in the year in which the companies first earn taxable income.

The proportion of the Company's taxable income entitled to benefits of reduced tax rates is calculated on the basis of the ratio between the turnover of the approved enterprise and the whole turnover of the Company. The turnover applicable to the approved enterprise is calculated, as a general rule, by taking the increase resulting from the comparison of the Company's turnover with its "base" turnover, which is prescribed as being the turnover during the last year before the operation of the approved enterprise, or such other basis as is stipulated in the instrument of approval.

The period of benefits in respect of certain enterprises expired in 1994, while the period of benefits in respect of other enterprises expires in 2006. The Company first derived income from approved enterprises in 1998.

In the event of distribution of cash dividends out of income, which was tax exempt as above, the companies would have to pay the 25% tax in respect of the amount distributed.

b) Accelerated depreciation

The companies are entitled to claim accelerated depreciation in respect of buildings, machinery and equipment used by approved enterprises during the first five tax years of the operation of these assets.

c) Conditions for entitlement to the benefits

The entitlement to the above benefits is conditional upon the companies fulfilling the conditions stipulated by the law, regulations published thereunder and the

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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 Israeli CPI and interest.

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DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 11 - TAXES ON INCOME (continued):

2) Measurement of results for tax purposes under the Income Tax (Inflationary Adjustments) Law, 1985 (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. Under income tax regulations, the Company and certain subsidiaries are entitled to adjust their results for tax purposes on the basis of the changes in the exchange rate of the dollar, instead of the changes in the Israeli CPI. Commencing 2001 the Company and two of its subsidiaries chose to do so.

As explained in note 1a(4), the financial statements were measured in dollars. For the years in which the result for tax purposes are measured in real terms, having regard to the changes in the Israeli CPI, the difference between the changes in the Israeli CPI and the exchange rate of the dollar - both on an annual and a cumulative basis - caused differences between taxable income and income reflected in these financial

statements. Paragraph 9(f) of FAS 109 creates an exception which prohibits the recognition of deferred tax liabilities or assets that arise from differences between the financial reporting and tax bases of assets and liabilities that are remeasured from the local currency into dollars using historical exchange rates, and that result from (i) changes in exchange rates, or (ii) indexing for tax purposes.

3) Tax rates

a) The income of the company and its Israeli subsidiaries (other than income from "approved enterprises", see 1a. above) is taxed at the regular rate. Through to December 31, 2004, 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 is 35%, and will be 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 of the amendment to the law, is included under the item "taxes on income" in the statements of income.

b) Pursuant to another amendment to the Income Tax Ordinance, which became effective in 2003, capital gains are taxed at a reduced rate of 25% from January 1, 2003, instead of the regular corporate tax rate at which such gains were taxed until the aforementioned date. The aforesaid amendment stipulates that with regard to the sale of assets acquired prior to January 1, 2003, the reduced tax rate will be applicable only for the gain allocated to capital gains earned after the implementation of the amendment, which will be calculated, as prescribed by said amendment.

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DELTA GALIL INDUSTRIES LTD..  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 11 - TAXES ON INCOME (continued):

4) Tax benefits under the Law for the Encouragement of Industry (Taxation), 1969

The Company and certain Israeli subsidiary are "industrial companies" as defined by this law. As such, these companies are entitled to certain tax benefits, consisting mainly of accelerated depreciation, as stipulated by regulations published under the inflationary adjustments law, and the right to claim

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public issuance expenses as a deduction for tax purposes.

Pursuant to this law, the Company files consolidated tax returns with the said subsidiary.

### B. NON-ISRAELI SUBSIDIARIES

Subsidiaries that are incorporated outside of Israel, except which incorporated in the free zone, are assessed for tax under the tax laws in their countries of residence. The principal tax rates applicable to main subsidiaries outside Israel are as follows:

Company incorporated in the USA - tax rate of 38%-40% Company incorporated in U.K- tax rate of 30%

### C. CARRYFORWARD TAX LOSSES

Carryforward tax losses (derived from the Israeli companies) as of December 31, 2004 and 2003, aggregate \$ 36 million and \$ 33 million, respectively.

Carryforward tax losses in Israel may be utilized indefinitely.

### D. DEFERRED INCOME TAXES:

1) The deferred income taxes are composed as follows:

|   | DECEMBER 31  |          |
|---|--------------|----------|
|   | 2004         | 2003     |
|   | IN THOUSANDS |          |
|   | -----        | -----    |
| Property, plant and equipment                           | \$13,832     | \$13,975 |
| Inventories   | (841)        | (907)    |
| Provisions for employee related obligations             | (1,457)      | (1,551)  |
| Other   | 653          | (639)    |
| In respect of carryforward tax losses<br>(see c. above) | (10,968)     | (10,042) |
| Total   | \$1,219      | \$836    |
|   | =====        | =====    |

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DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 11 - TAXES ON INCOME (continued):

2) Deferred income taxes are presented in the balance sheets among:



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|                     | DECEMBER 31  |            |
|---------------------|--------------|------------|
|                     | 2004         | 2003       |
|                     | IN THOUSANDS |            |
| Current asset       | \$ (3,675)   | \$ (5,464) |
| Long term liability | 4,894        | 6,300      |
|                     | \$1,219      | \$836      |

E. INCOME BEFORE INCOME TAXES IS COMPOSED AS FOLLOWS:

|  | YEAR ENDED DECEMBER 31 |            |            |
|--|------------------------|------------|------------|
|  | 2004                   | 2003       | 2002       |
|  | IN THOUSANDS           |            |            |
| The Company and its Israeli Subsidiaries | \$3,190                | \$ (4,832) | \$ (8,658) |
| Non-Israeli subsidiaries                 | 13,946                 | 36,263     | 31,930     |
|  | \$17,136               | \$31,431   | \$23,272   |

F. TAXES ON INCOME INCLUDED IN THE STATEMENTS OF INCOME:

|                      | YEAR ENDED DECEMBER 31 |            |            |
|----------------------|------------------------|------------|------------|
|                      | 2004                   | 2003       | 2002       |
|                      | IN THOUSANDS           |            |            |
| Current:             |                        |            |            |
| Israeli              | \$1,636                | \$746      | \$353      |
| Non-Israeli          | 1,941                  | 10,292     | 4,963      |
|                      | 3,577                  | 11,038     | 5,316      |
| Deferred:            |                        |            |            |
| Israeli              | \$ (498)               | \$ (4,075) | \$ (1,796) |
| Non-Israeli          | 219                    | 520        | 2,236      |
|                      | (279)                  | (3,555)    | 440        |
| For previous years : |                        |            |            |
| Israeli              | \$ (516)               | \$ (30)    | \$ (112)   |
| Non-Israeli          | 64                     | (113)      | 135        |

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|         |         |         |
|---------|---------|---------|
| (452)   | (143)   | 23      |
| -----   | -----   | -----   |
| \$2,846 | \$7,340 | \$5,779 |
| =====   | =====   | =====   |

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DELTA GALIL INDUSTRIES LTD.  
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 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 11 - TAXES ON INCOME (continued):

- G. Following is a reconciliation of the theoretical tax expense, assuming all income is taxed at the regular tax rates applicable to income of companies in Israel (36% in the years 2002 and 2003, and 35% in 2004) and the actual tax expense:

|   | YEAR ENDED DECEMBER |          |
|---|---------------------|----------|
|   | 2004                | 2003     |
|   | -----               | -----    |
|   | IN THOUSANDS        |          |
|   | -----               | -----    |
| Income before taxes on income, as reported in the consolidated statements of income   | \$17,136            | \$31,400 |
| Theoretical tax expense   | \$5,997             | \$11,300 |
|   | =====               | =====    |
| Additional tax expenses arising from reduced tax rate on losses from an approved enterprise   | 73                  | 300      |
| Decrease in tax arising from different tax rate applicable to non-Israeli subsidiaries  | (2,575)             | (2,830)  |
|   | -----               | -----    |
|   | 3,495               | 8,800    |
| Increase (decrease) in taxes resulting from\ permanent differences:   |                     |          |
| Disallowable deductions   | 110                 |          |
| Previous years  | (452)               | (1400)   |
| Difference between the basis of measurement of income reported for tax purposes and the basis of measurement of income for financial reporting purposes - net | (807)               | 1000     |
| Sundry - net  | 500                 | (1,560)  |
|   | -----               | -----    |
| Taxes on income - in the consolidated statements of income  | \$2,846             | \$7,300  |
|   | =====               | =====    |

H. TAX ASSESSMENTS

Tax assessments for the Company and most of its subsidiaries are final through the tax year 1999.

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DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 12 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION:

BALANCE SHEETS:

|  | DECEMBER 31  |          |
|--|--------------|----------|
|  | 2004         | 2003     |
|  | IN THOUSANDS |          |
| A. ACCOUNTS RECEIVABLE:                                    |              |          |
| 1) Trade:  |              |          |
| Outside Israel   | \$90,682     | \$73,883 |
| In Israel  | 14,447       | 11,840   |
|  | -----        | -----    |
|  | \$105,129    | \$85,723 |
|  | =====        | =====    |
| Allowance for doubtful accounts:                           |              |          |
| Opening balance  | \$1,038      | \$1,131  |
| Hamashbir  |              |          |
| Other  |              |          |
| Decrease due to bad debts                                  |              |          |
| Hamashbir  | (872)        |          |
| K-Mart   |              |          |
| Other  | (39)         | (123)    |
| Increase due to an acquisition of a new subsidiary         |              | 30       |
|  | -----        | -----    |
| Closing balance  | \$127        | \$1,038  |
|  | =====        | =====    |
| Principal customers (see note 1m and 15c):                 |              |          |
| Customer 1   | \$2,656      | \$18,890 |
|  | =====        | =====    |
| Customer 2   | \$29,871     | \$15,907 |
|  | =====        | =====    |
| Customer 3   | \$15,455     | \$16,500 |
|  | =====        | =====    |
| 2) Other:  |              |          |
| Investment grant receivable                                | \$646        | \$576    |
| Government departments - mainly value added tax refundable | 1,501        | 4,500    |
| Prepaid expenses   | 1,822        | 2,046    |
| Deposits   | 858          | 663      |
| Income receivable  | 1,184        | 96       |
| Employees  | 380          | 512      |
| Receivables from subcontractors                            | 2,987        | 1,157    |
| Sundry   | 1,249        | 1,112    |
|  | -----        | -----    |
|  | \$10,627     | \$10,662 |
|  | =====        | =====    |

DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

## NOTE 12 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

|    |                                     | DECEMBER 31  |           |
|----|-------------------------------------|--------------|-----------|
|    |                                     | 2004         | 2003      |
|    |                                     | IN THOUSANDS |           |
|    |                                     | -----        | -----     |
| B. | INVENTORIES:                        |              |           |
|    | Finished products                   | \$137,813    | \$94,338  |
|    | Products in process                 | 21,829       | 21,380    |
|    | Raw materials and supplies          | 12,797       | 19,918    |
|    | Packaging and maintenance materials | 11,328       | 7,348     |
|    |                                     | -----        | -----     |
|    |                                     | \$183,767    | \$142,984 |
|    |                                     | =====        | =====     |

## C. SHORT-TERM BANK CREDIT

The weighted average interest rate of short-term bank credit as of December 31, 2004 and 2003 is 3.5% and 1.9% , respectively. A subsidiary is a party to a credit agreement, which was amended, as of December 9 2004, with Bank Leumi U.S.A and Bank Hapoalim B.M. Borrowings under the credit agreement are secured by substantially all of the assets of the subsidiary. The credit agreement provides for up to \$ 60 million in short term credit (see note 8e).

Unutilized short-term credit lines of the Group (under the USA credit agreement and other credit agreements) as of December 31, 2004 and 2003 aggregated to \$ 163 million and \$ 100 million, respectively.

|    |   | DECEMBER 31  |         |
|----|---|--------------|---------|
|    |   | 2004         | 2003    |
|    |   | IN THOUSANDS |         |
|    |   | -----        | -----   |
| D. | ACCOUNTS PAYABLE AND ACCRUALS - OTHER:    |              |         |
|    | Employees and employee institutions       | \$7,745      | \$7,589 |
|    | Provision for vacation and recreation pay | 4,297        | 4,463   |
|    | Income tax payable                        | 2,731        | 1,612   |
|    | Accrued expenses                          | 18,300       | 17,956  |

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|   |          |          |
|---|----------|----------|
| Accrued expenses - restructuring costs                  |          | 6,163    |
| In respect of purchase price adjustment,<br>see note 2f |          | 6,700    |
| In respect of derivatives, see note 13c                 |          | 2,657    |
| Other   | 1,010    | 1,002    |
|   |          | -----    |
|   | \$34,083 | \$48,142 |
|   | =====    | =====    |

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DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 12 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

STATEMENTS OF INCOME:

E. RESTRUCTURING EXPENSES

1) Consolidated statements of operations for the years ended December 31, 2004, 2003 and 2002 include restructuring costs in the Europe segment totaling approximately \$1.1 million \$1.0 million and \$1.1 million respectively. During the years ended December 31, 2004, 2003 and 2002, the Company implemented restructuring plans which included the dismissal of a total of approximately 1,300 employees and the closing of certain of the Company's sewing plants and logistic centers.

2) The primary components of the restructuring costs are:

|   | YEAR ENDED DECEMBER 31 |         |         |
|---|------------------------|---------|---------|
|   | 2004                   | 2003    | 2002    |
|   | -----                  | -----   | -----   |
|   | IN THOUSANDS           |         |         |
|   | -----                  | -----   | -----   |
| Costs relating to workforce reduction                       | \$190                  | \$850   | \$651   |
| Costs relating to write-off of fixed assets                 | 50                     | 157     | 414     |
| Costs relating to write-off of other<br>accounts receivable | 860                    |         |         |
|   | -----                  | -----   | -----   |
|   | \$1,100                | \$1,007 | \$1,065 |
|   | =====                  | =====   | =====   |

THE 2004 PROGRAM

During the fourth quarter of 2004 the Company initiated a restructuring program designed to reduce its cost structure (the "2004 Program"). The 2004 Program included the closure of a logistic center in Hungary and resulted in total restructuring costs of \$1.5 million, from which \$0.4 million included among cost of sales (related to inventory).

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The implementation of the 2004 Program in Hungary, consisted of the dismissal of approximately 230 persons who had previously been employed by the Company's Hungary subsidiary. The 2004 Program was concluded by May 2005.

### THE 2003 PROGRAM

During 2003, the Company initiated a restructuring program designed to reduce its cost structure (the "2003 program"). The 2003 Program included the closure of sewing plants in Scotland and in Israel. The 2003 Program resulted in total restructuring charges to the Company of \$1.0 million, which were recorded in the first quarter of 2003.

The implementation of the 2003 Program in Scotland, which represented \$0.9 million of the total charges of \$1.0 million, consisted of the dismissal of approximately 100 persons who had previously been employed by the Company's European subsidiary.

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DELTA GALIL INDUSTRIES LTD.

(An Israeli corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

### NOTE 12 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

The implementation of the 2003 Program in Israel which represented \$0.1 million of the total charges of \$1.0 million, consisted of the dismissal of approximately 70 employees in Israel, who had previously been employed by the Company's. 2003 Program was concluded by the end of the first quarter of 2003.

### THE 2002 PROGRAM

During 2002, the company initiated restructuring program designed to reduce its cost structure (the "2002 program"). The 2002 program included the closure of cutting and sewing facilities in Scotland and in the Dominican Republic. The 2002 program resulted in total restructuring charges to the Company of \$1.1 million which were recorded in the fourth quarter of 2002.

The implementation of the 2002 program in Scotland, which represented \$0.7 million of the total \$1.1 million, consisted of the dismissal of approximately 100 employees in Scotland.

The implementation of the 2002 program in Dominican Republic, which represented \$0.4 million of the total \$1.1 million, consisted of the dismissal of approximately 800 employees in the Dominican Republic.

As to restructuring plan with respect to an acquiree company, in 2003, see note 2c.

F. FINANCIAL EXPENSES - NET:

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|                                      | YEAR ENDED DECEMBER 31 |         |         |
|--------------------------------------|------------------------|---------|---------|
|                                      | 2004                   | 2003    | 2002    |
|                                      | IN THOUSANDS           |         |         |
| Interest expenses                    | \$4,923                | \$3,824 | \$4,286 |
| Interest income                      | (42)                   | (58)    | (92)    |
| Exchange differences and other - net | 763                    | 1,259   | 939     |
| Losses from derivatives instruments  | 587                    | 612     | 323     |
|                                      | \$6,231                | \$5,637 | \$5,456 |

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 12 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

G. EARNINGS PER SHARE

Following is data relating to the weighted average number of shares used in the computation of diluted earnings per share:

|   | 2004         | 2003   | 2002  |
|---|--------------|--------|-------|
|   | IN THOUSANDS |        |       |
| Weighted average number of shares used in the computation of basic earnings per share   | 18,478       | 18,313 | 18,91 |
| Add:  |              |        |       |
| Net additional shares from the anticipated exercise of stock options                    | 356          | 450    | 1     |
| Weighted average number of shares used in the computation of diluted earnings per share | 18,834       | 18,763 | 18,92 |

NOTE 13 - FINANCIAL INSTRUMENTS AND RISK MANAGEMENT:

A. GENERAL

The Group operates internationally, which gives rise to exposure to market risks mainly from changes in exchange rates of foreign currencies in relation to the dollar. Derivative financial instruments ("derivatives") are utilized by the Group to reduce these risks, as explained in this note. As the counter parties

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to these derivatives are Israeli banks, the Company considers the inherent credit risks remote. The Company does not hold or issue derivative financial instruments for trading purposes.

### B. FOREIGN EXCHANGE RISK MANAGEMENT

The Company enters into most foreign currency derivatives - forward exchange contracts - in order to protect itself from the risk that the eventual non-dollar net cash flows resulting from sales of products and from salaries, wages and related expenses, will be affected by changes in exchange rates. The term of most of these contracts is less than one year.

These transactions are mainly for the exchange of pounds sterling, Euro and NIS into dollars.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 13 - FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued):

For forward exchange contracts designated as cash flow hedges, gains and losses are recorded in other comprehensive income (loss) until the foreign currency denominated sales, salaries, wages and related expenses transactions are recognized in earnings.

The following table summarizes changes in other comprehensive income (loss) related to derivatives that are classified as cash flow hedges held by the Company during the period from January 1, 2002 through December 31, 2004:

|   | 2004            | 2003      |
|---|-----------------|-----------|
|   | -----           | -----     |
|   | \$ IN THOUSANDS |           |
|   | -----           | -----     |
| Balance at beginning of year  | \$(1,715)       | \$(583)   |
| Changes in effective portion of derivatives<br>designated as cash flow hedges | 691             | (2,905)   |
| Reclassification into earnings from other<br>comprehensive income             | 1,822           | 1,299     |
| Net of tax effect   | (798)           | 474       |
|   | -----           | -----     |
| Balance at end of year  | -;-             | \$(1,715) |
|   | =====           | =====     |

Hedge loss related to the portion of cash flow hedging instruments excluded from assessment of effectiveness had impact on earnings for 2004 of \$ 0.6 million, 2003 of \$ 0.7 million loss and had no material impact on earnings for the years ended December 31, 2002. No cash flow hedges were discontinued during the years ended December 31, 2004, 2003 and 2002.



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As of December 31, 2004, the Company has no derivatives instruments outstanding.

### C. FAIR VALUE OF FINANCIAL INSTRUMENTS

The financial instruments of the Group consist mainly of non-derivative assets and liabilities (items included in working capital, long-term receivables - in insignificant amounts - and long-term liabilities); the Group also has derivatives.

In view of their nature, 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 long-term receivables and long-term loans also approximates their carrying value, since they bear interest at rates close to the prevailing market rates, or are in immaterial amounts. The fair values derivatives as of December 31, 2003 was \$ 2,657 thousands (As of December 31, 2004, the Company has no derivative instruments).

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

#### NOTE 14 - "RELATED PARTIES" - TRANSACTIONS AND BALANCES:

##### A. TRANSACTIONS WITH RELATED PARTIES:

|                              | YEAR ENDED DECEMBER 31 |         |         |
|------------------------------|------------------------|---------|---------|
|                              | 2004                   | 2003    | 2002    |
|                              | IN THOUSANDS           |         |         |
| Net revenues                 | \$1,303                | \$2,433 | \$4,922 |
| Purchases and other expenses | \$21                   | \$249   | \$410   |

The above transactions were made with one of the Company's shareholders in the ordinary course of business, at prices agreed upon in negotiations between the parties, taking into account the volume of orders, at customary supplier credit terms.

As to options granted to the Company's CEO, see note 10b.

##### B. RELATED PARTIES BALANCES:

DECEMBER 31

|   | 2004         | 2003  |
|---|--------------|-------|
|   | IN THOUSANDS |       |
| Current receivables - presented in the balance sheets among "accounts receivable - trade" | \$126        | \$251 |
| Current liabilities - presented under "accounts payable and accruals"                     | \$20         | \$28  |

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 15 - SEGMENT INFORMATION :

A. INFORMATION ON OPERATING SEGMENTS:

OPERATING SEGMENTS:

1) General:

The Company conducts its worldwide operations in five operating segments as follows:

Delta USA, U.S upper market and Europe- these segments are engaged in manufacturing and marketing of intimate apparel to various customers in the U.S and European markets. Socks- the segment is engaged in manufacturing and marketing of socks to various customers in the U.S and European markets. Delta marketing Israel - this segment is engaged in marketing of intimate apparel to various customers in Israel through retail and wholesale operations.

The Company changed its internal organization by transferring Socks marketing operation in Israel to the managerial responsibility of Delta Marketing Israel. In addition, US upper market and the textile divisions were merged. Numbers included below have been reclassified accordingly.

2) Information on revenues, profit (losses) and assets of the reportable operating segments:

a) Measurement of revenues, profit (losses) and assets of the operating segments:

The measurement of revenues, profit (losses) and assets of the reportable operating segments is

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based on the same accounting principles applied in these financial statements, except for:

- 1) The effect of hedging transactions that were excluded from segment data.
- 2) The Company fully consolidates the operating results of certain subsidiary in its consolidated financial statements, while for operating segment data the Company includes only its share (approximately 50.1%) in the operating profits of this subsidiary as part of the US Upper market segment.

Segment profits (losses) reflect the income (loss) from operations of the segment and do not include financial expenses, other income, income tax expenses, share in profits (losses) of associated companies and minority interest, since those items are not allocated to the segments. Sale price of intersegment revenue is based on negotiation between the segments and when applicable upon market price.

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DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 15 - SEGMENT INFORMATION (continued):

b) Financial data relating to reportable operating segments:

|                               | DELTA USA<br>-----     | US UPPER<br>MARKET<br>----- | EUROPE<br>----- | SOCKS<br>----- | DELTA<br>MARKET<br>ISRAELI<br>----- |
|-------------------------------|------------------------|-----------------------------|-----------------|----------------|-------------------------------------|
|                               | (U.S. \$ IN THOUSANDS) |                             |                 |                |                                     |
| Year ended December 31, 2004: |                        |                             |                 |                |                                     |
| Net revenues:                 |                        |                             |                 |                |                                     |
| To unaffiliated customers     | \$186,280              | \$90,540                    | \$193,638       | \$138,749      | \$46,4                              |
| Intersegment                  |                        | \$21,312                    | \$165           | \$5,435        |                                     |
| Total net revenues            | \$186,280              | \$111,852                   | \$193,803       | \$144,184      | \$46,4                              |
| Operating income (loss)       | \$5,911                | \$(568)                     | \$4,906(4)      | \$9,137        | \$4,7                               |
| Assets (at end of year)       | \$225,744              | \$98,055                    | \$100,264       | \$56,271       | \$23,8                              |
| Depreciation and amortization | \$1,438                | \$6,097                     | \$4,326         | \$2,463        | \$4                                 |

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- (1) Includes results of hedge transactions.
- (2) Includes mainly the effect of hedge transactions in an amount of \$1,700 thousands.
- (3) Includes general corporate assets not assignable to segments.
- (4) Includes restructuring expenses in the amount of \$1,500 thousands relating to the closure

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DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 15 - SEGMENT INFORMATION (continued):

|                               | DELTA USA              | US UPPER<br>MARKET | EUROPE      | SOCKS    | DELTA<br>MARKET<br>ISRAEL |
|-------------------------------|------------------------|--------------------|-------------|----------|---------------------------|
|                               | (U.S. \$ IN THOUSANDS) |                    |             |          |                           |
| Year ended December 31, 2003: |                        |                    |             |          |                           |
| Net revenues:                 |                        |                    |             |          |                           |
| To unaffiliated customers     | \$213,241              | \$66,665           | \$176,827   | \$86,393 | \$37,5                    |
| Intersegment                  |                        | 21,603             | 563         | 3,022    |                           |
| Total net revenues            | \$213,241              | \$88,268           | \$177,390   | \$89,415 | \$37,5                    |
| Operating income (loss)       | \$24,780               | \$ (8,871)         | \$4,453 (4) | \$8,997  | \$2,4                     |
| Assets (at end of year)       | \$137,762              | 84,185             | \$109,377   | \$69,877 | \$19,7                    |
| Depreciation and amortization | \$1,561                | \$5,560            | \$4,368     | \$2,148  | \$3                       |

- (1) Includes results of hedge transactions.
- (2) Including mainly capital gain in an amount of \$ 4,050 thousands, the effect of losses of hedge \$ 1,300 thousands and gain of \$600 thousands which represents the minority share in the open subsidiary - included in the US Upper market - which is partly consolidated for segment purpose consolidated financial statements.
- (3) Includes general corporate assets not assignable to segments.
- (4) Includes restructuring expenses in the amount of \$ 1,007 thousands relating to the closure of in Israel.

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DELTA GALIL INDUSTRIES LTD.  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

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NOTE 15 - SEGMENT INFORMATION (continued):

|                               | DELTA USA              | US UPPER<br>MARKET | EUROPE    | SOCKS    | DELTA<br>MARKET<br>ISRAEL |
|-------------------------------|------------------------|--------------------|-----------|----------|---------------------------|
|                               | (U.S. \$ IN THOUSANDS) |                    |           |          |                           |
| Year ended December 31, 2002: |                        |                    |           |          |                           |
| Net revenues:                 |                        |                    |           |          |                           |
| To unaffiliated customers     | \$202,024              | \$81,968           | \$170,265 | \$79,193 | \$34,8                    |
| Intersegment                  |                        | 29,157             | 706       | 4,710    |                           |
| Total net revenues            | \$202,024              | \$111,125          | \$170,971 | \$83,903 | \$34,8                    |
| Operating income (loss) (3)   | \$14,575               | \$(4,731)          | \$10,205  | \$8,319  | \$(1,2                    |
| Assets (at end of year)       | \$143,730              | \$94,849           | \$105,522 | \$46,413 | \$17,1                    |
| Depreciation and amortization | \$1,294                | \$5,518            | \$3,932   | \$2,420  | \$3                       |

- (1) Includes results of hedge transactions.  
(2) Includes general corporate assets not assignable to segments.  
(3) Includes restructuring costs in the amount of \$ 673 thousands in Europe and \$ 392 thousands  
(4) Including mainly the losses of hedge transactions in an amount of \$ 960 thousands and gains represents the minority share in the operating profits of certain subsidiary - included in the partly consolidated for segment purposes and fully consolidated in the consolidated financial statements.

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DELTA GALIL INDUSTRIES LTD.  
(An Israeli corporation)  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 15 - SEGMENT INFORMATION (continued):

B. GEOGRAPHICAL INFORMATION:

|   | YEAR ENDED DECEMBER 31 |           |           |
|---|------------------------|-----------|-----------|
|   | 2004                   | 2003      | 2002      |
|   | IN THOUSANDS           |           |           |
| 1) Revenues attributed to geographic area (based on the location of the customers): |                        |           |           |
| North America   | \$334,833              | \$300,708 | \$303,103 |

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|                          |           |           |           |
|--------------------------|-----------|-----------|-----------|
| United Kingdom           | 202,831   | 187,885   | 181,302   |
| Europe (other than U.K.) | 64,605    | 48,766    | 44,409    |
| Israel                   | 52,000    | 42,771    | 38,484    |
|                          | -----     | -----     | -----     |
|                          | \$654,269 | \$580,130 | \$567,298 |
|                          | =====     | =====     | =====     |

- 2) The net balance of the Company's property, plant and equipment, by geographic location, are as follows:

|                | DECEMBER 31  |           |           |
|----------------|--------------|-----------|-----------|
|                | 2004         | 2003      | 2002      |
|                | -----        | -----     | -----     |
|                | IN THOUSANDS |           |           |
|                | -----        | -----     | -----     |
| Israel         | \$57,685     | \$60,108  | \$64,998  |
| Egypt          | 24,464       | 22,218    | 20,940    |
| United States  | 15,637       | 8,369     | 7,284     |
| Eastern Europe | 11,370       | 11,719    | 6,803     |
| Jordan         | 9,470        | 9,666     | 10,510    |
| United Kingdom | 3,831        | 4,429     | 7,740     |
| Ireland        | 1,184        | 5,450     |           |
| Thailand       | 2,108        |           |           |
| Other          | 2,592        | 2,918     | 3,326     |
|                | -----        | -----     | -----     |
|                | \$128,341    | \$124,877 | \$121,601 |
|                | =====        | =====     | =====     |

C. REVENUES FROM PRINCIPAL CUSTOMERS:

|            | YEAR ENDED DECEMBER 31 |           |           |
|------------|------------------------|-----------|-----------|
|            | 2004                   | 2003      | 2002      |
|            | -----                  | -----     | -----     |
|            | IN THOUSANDS           |           |           |
|            | -----                  | -----     | -----     |
| Customer 1 | \$188,947              | \$179,120 | \$174,195 |
| Customer 2 | \$86,177               | \$82,472  | \$76,910  |
| Customer 3 | \$70,157               | \$86,829  | \$65,317  |

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NOTE 16- SUBSEQUENT EVENT

A. During the third quarter of 2005, as a result of a change in the business environment and the erosion in selling prices, the Company's management implemented a restructuring plan in order to reduce expenses and improve efficiency of operations. In the third quarter of 2005, the Company recorded expenses relating to the restructuring plan at the total amount of \$ 8.6 million. This plan includes the costs associated with closing certain

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manufacturing plants in Central and North America and in Israel and the related employee termination accruals.

In addition to the restructuring plan, the Company recorded in the third quarter of 2005 an impairment of long-lived assets pursuant to FAS No. 144 "Accounting for the Impairment or Disposal of Long-Lived Assets" in an amount of \$ 7.4 million, and a further goodwill impairment pursuant to FAS No. 142 "Goodwill and Other Intangible Assets" in an amount of \$ 5.5 million.

B. A subsidiary of the Company is a party to a credit agreement, which provides for \$ 130 million in loans, of which \$ 70 million are long term loans which bear interest of Libor +1.4% and the remainder is short term credit which bears interest of Libor +1.15%. The principal of the term loans is payable in 20 equal quarterly installments. This credit agreement includes covenants based on the ratio of the subsidiary's EBITDA to fixed charges, the ratio of net worth to total assets of the subsidiary and the ratio of the sum of the subsidiary's (a) loans (b) letters of credit, and (c) acceptances (or, collectively, debt) to EBITDA.

The subsidiary and the banks amended the credit agreement in January 12, 2006. The material changes contained in the amendment are the following:

- o An increase in the interest rate on the revolving credit from LIBOR plus 1.15% to LIBOR plus 1.40%, and an increase in the interest rate on the term loan from LIBOR plus 1.40% to LIBOR plus 1.65%;
- o A prepayment of \$25 million of the principal amount of the term loan;
- o A reduction in the quarterly payment on the term loan from \$3.5 million to \$1.9 million; and
- o An extension of the expiration of the revolving loan facility from January 15, 2006 to May 15, 2006.

The subsidiary did not satisfy the covenant relating to the ratio of EBITDA to fixed charges for the year ended December 31, 2005. The amendment, from January 12, 2006, provided for a waiver of all of the financial covenants for the period ending December 31, 2005.

The company is in the process of negotiation with the banks to amend the ratio of the credit agreement to new covenant targets.

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### Report of Independent Auditors

The Board of Directors of Delta Textile Egypt - Free Zone (S.A.E.)

We have audited the balance sheets of Delta Textile Egypt - Free Zone (S.A.E.) as of 31 December 2004 and 2003, and the related statements of income, shareholders' equity, and cash flows for each of the three years in the period ended 31 December 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 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

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statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits 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 Group'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 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 Delta Textile Egypt - Free Zone (S.A.E.) at 31 December 2004 and 2003, and the results of its operations and its cash flows for each of the three years in the period ended 31 December 2004, in conformity with the Egyptian Accounting Standards and the related applicable Egyptian laws and regulations which differ in certain respects from United States generally accepted accounting principles (see Note 14 of Notes to the Financial Statements).

Allied for Accounting and Auditing-  
Member Firm of Ernst & Young Global

Cairo, Egypt  
30 March 2006

### Report of Independent Auditors

The Board of Directors of Delta Egypt Sourcing (Limited Liability Company)

We have audited the balance sheets of Delta Egypt Sourcing (Limited Liability Company) as of 31 December 2004 and 2003, and the related statements of income and changes in Quota holders' Equity and cash flows for each of the three years in the period ended 31 December 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 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 audits 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 Group'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 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 Delta Egypt Sourcing (Limited Liability Company) at 31 December 2004 and 2003, and the results of its operations and cash flows for each of the three years in the period ended



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December 31, 2004, in conformity with the Egyptian Accounting Standards and the related applicable Egyptian laws and regulations which differ in certain respects from United States generally accepted accounting principles (see Note 12 of Notes to the Financial Statements).

Allied for Accounting and Auditing-  
Member Firm of Ernst & Young Global

Cairo, Egypt  
30 March 2006

### REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM TO THE MEMBERS OF DELTA TEXTILES (LONDON) LIMITED

We have audited the balance sheets of Delta Textiles (London) Limited and its subsidiaries ("the Company") as at 31 December 2004 and 31 December 2003 and the related statements of income, changes in shareholder equity and cash flows for each of the three years in the period ended 31 December 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 generally accepted auditing standards in the United Kingdom and 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 from 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 the significant estimates made by the Company's Board of Directors and management, as well as evaluating the overall annual accounts presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the aforementioned financial statements present fairly, in all material respects, the financial position of the Company as at 31 December 2004 and 31 December 2003 and the result of its operations, changes in its shareholders' equity and cash flows for each of the three years in the period ended 31 December 2004, in conformity with generally accepted accounting principles in the United Kingdom. In addition they present fairly, in all material respects, the financial position of the Company as at 31 December 2004 and 31 December 2003 and the results of its operations for each of the three years in the period ended 31 December 2004, in conformity with generally accepted accounting principles in the United States of America.

BAKER TILLY

Registered Auditor  
Chartered Accountants  
2 Bloomsbury Street  
London WC1B 3ST  
United Kingdom

10 April 2006