UPGRADING EVERYDAY SECURITY

2013 Annual Report Management Discussion and Analysis (the "Report")

1. Operational Activities

1.1 Business Overview

Electronics Line 3000 Ltd. (“EL” or the “Company”) is a pioneer in next-generation security solutions for the residential and small commercial markets. The Company designs and produces cutting-edge solutions for security and control of living and working environments. The EL line provides comprehensive security protection, as well as sophisticated system and home management functionality, for optimal comfort, safety and peace of mind. This new industry standard is further upgraded with enhanced remote management capabilities that give homeowners instant access to their system from anywhere in the world.

Upgrading Everyday Security

EL solutions enable new levels of control and maintenance in protected sites through ELAS, a proprietary remote management server. The Company enjoys a unique market position in supplying ELAS-governed systems for the home and workplace, which provide the multiple benefits of a virtual security presence, convenient home automation, and energy efficiency, all customized by the end-user and/or the service provider.

EL’s extensive product line includes both wired and wireless solutions. EL solutions offer enhanced detection and PSTN/IP/GSM/GPRS-based event reporting, along with advanced remote management tools. Effective back-office support and customized branding of EL solutions provide superior security with significant business benefits and market expansion potential.

Global Partnerships

Nearly three decades of cutting-edge leadership have earned EL a solid market position, allowing users worldwide to benefit from EL's ongoing development of upgraded security solutions. The Company maintains long-term partnerships worldwide.

EL has made cutting-edge technology, user-friendly design and exceptional quality the benchmarks for serving its international network of clients and partners. Drawing on a tradition of pioneering expertise, EL specialists also provide security integration consultancy, installation service, training and technological support.

EL was established in 1982 and is headquartered in Israel. The Company is publicly traded on the Frankfurt Stock Exchange (ELN) and is part of the RISCO Group, an established leader in the international security market.

In March 2010 RISCO Ltd., ("Risco") a leading provider of integrated security solutions, acquired a controlling interest in the Company. RISCO Group intends to maintain the Company's product offerings and independence in the market by growing it as RISCO Group's residential arm through product portfolio expansion into video and management solutions together with its major partners worldwide.

In order to increase the Company's global coverage and to have better penetration into new and existing markets, in August 2010, the Company entered into management and distribution agreements with Risco as Risco has the facilities to import, promote, sell, market and distribute the products in the territory (as defined in the agreement) and is willing to act as the supplier's non-exclusive distributor of the "Products in the Territory".

The Company reorganized its sales force in order to achieve a better coverage in its target markets. Mr. Douglas Luscombe, the Company's CEO, was located in the UK and several regional Sales Managers (RSM) were assigned to cover the rest of Europe and the Russian markets.

The Company has a presence, and believes it is well positioned in important markets around the world, in particular Northern and Western Europe and consistently strengthening its position in additional regions in Latin America, APAC and more. The Company's brand is associated with high quality products and solutions.

The Company continues to develop and expand its marketing and sales capabilities with a focus on strategic customers and markets, while at the same time, providing more marketing and technical support to existing customers.

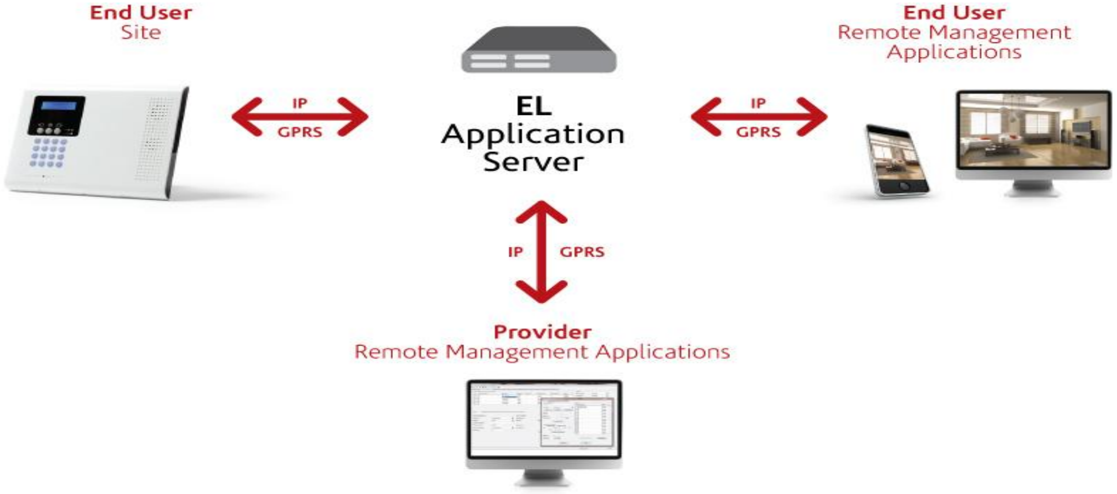
Products and Product Families

The Company offers an array of security solutions for every need. EL's wireless control systems enable end-users to choose the level of control and monitoring they require using innovative remote solutions.

Advanced security detectors supply excellent interior and perimeter protection while safety detectors offer enhanced environmental and personal safety including: smoke, gas and water leak detection, panic buttons and much more.

The systems can be activated using a variety of local control devices such as keyfobs and keypads. EL also offers end-users and providers advanced remote management applications for comprehensive control over the system from any location.

Complementing accessories and add-ons include home automation modules, zone expanders, receivers, sirens and the more for a complete security offering.



ELAS (Electronics-Line Application Server) is EL's cloud-based server which enables EL's intrusion systems to be controlled remotely using the [MyELAS]smartphone app.

ELAS acts as a proxy that mediates between the various applications and the panels. When the end-user exerts the MyELAS app, the application connects to ELAS and ELAS in turn connects to its main panel. Data is then transferred between the panel and the smartphone in real-time.

Smartphone App

The MyELAS app enables end-users to control their EL intrusion systems remotely, directly from their smartphones or via the web application with the push of a button, giving them peace of mind at all times.

Remote Configuration and Diagnostics

ELAS enables remote configuration and diagnostics, providing a more efficient way for installers to troubleshoot and solve issues without the need for extraneous onsite visits.

UPGRADING EVERYDAY SECURITY

Utilizing the most Stringent Security Technologies

ELAS utilizes security technologies including encryption, advanced firewalls and additional security safeguards that comply with the most rigorous security standards to ensure that data cannot be accessed by unauthorized users.

Reliable and Scalable

Our ELAS cloud server offers total reliability with full redundancy during server downtime, enabling seamless operation in times of crisis. The system offers a totally scalable architecture, i.e. the ability to easily increase the capability of the server with the growth of your company.

iConnect 2-Way is a powerful and streamlined 2-way wireless intrusion system, designed for the residential and small commercial markets.

Connection to the cloud-based ELAS server enables users to remotely control their iConnect 2-Way systems through the myELAS app (also available via web browser). Visual verification is also supported with the purchase of a PIR camera detector enabling users to view images on demand of their homes or businesses directly from their smartphones, allowing them to feel totally in control at all times. Users will receive email/ SMS/ voice notifications in the event of an alarm, and can also arm or disarm their iConnect 2-Way systems remotely.

iConnect 2-Way supports GPRS with GSM and IP as backup or IP and PSTN as backup, and can be remotely configured saving installers time and hassle. A wide range of 2-way detectors and accessories can be used with the system.

commpact

The **Commpact** intrusion system is named for its streamlined, space-saving design, while offering a professional, highly reliable system at a competitive price.

Commpact's connectivity to the cloud-based ELAS server enables it to be controlled remotely by EL's smartphone app (also available via web browser) which offers users the possibility to arm/disarm the system remotely as well as to receive email/ SMS/ voice notifications and to view and store a history of events.

Commpact supports a wide range of security and safety accessories including elderly care and detectors against smoke, flood and poisonous gases.

The simple and quick wireless installation and remote programming of the Commpact system add further to its appeal as a powerful, convenient system which allows users to enjoy a complete sense of control as well as peace of mind.

prime

Prime is a basic, reliable and robust security system using one-way wireless FM technology. The system uses PSTN and GSM connectivity and is compatible with all of EL's wireless keypads and peripherals. Prime supports variable applications such as SMS event notifications, remote programming and maintenance, audio communication or range extension.

1.2 Business Strategy

The Company is engaged in the design, development, production, marketing and sales of next-generation security solutions for the residential and small commercial markets.

The Company's vision is to be a leading global provider of wireless security with remote management solutions for the mass residential and small commercial markets.

Key elements of the Company's growth strategy include:

- Continuing to position the Company's advanced 2way wireless products as an innovative quality solution that reduces operating expenses for the service provider and increases functionality and control for the end user.
- Expanding and strengthening relationships with key target customers in order to sell wireless security with remote management solutions to their customers.
- Providing a full range of market solutions – from standard, low cost solutions to high end, advanced solutions.
- Increasing services which are available as part of the Company's platform for remote management solutions, including advanced video capabilities, remote management applications and the more.
- Leveraging wireless technology and various platforms to develop new solutions.
- Invest in both short-term and long-term R&D in order to improve product design and achieve lower production costs.

1.3 Information on the stock

The issued share capital of the company is NIS 68,564,240 and consists of 13,712,848 ordinary shares at a par value of NIS 5.00 each. All shares have the same voting rights and dividend claims.

There are no shares in the company with special rights according rights of control.

Under the provisions of German securities trading legislation, every investor whose proportion of the voting rights in the company reaches, exceeds or falls below certain thresholds as a result of the purchase or sale of shares or in any other way must notify the company and the Federal Financial Supervisory Authority (BaFin) thereof. The lowest threshold for such disclosures is 3%. Risco Ltd. currently holds more than 50% of the Company's share capital.

Restrictions on the voting rights of shares could result from statutory provisions. The Company's Board of Directors is not aware of any other restrictions on the exercise of voting rights or the transfer of shares.

The Company's shares are listed in the Prime Standard segment of the Frankfurt Stock exchange.

2. Economic Review

2.1 General economic conditions

Global activity strengthened during the second half of 2013 and is expected to improve further in 2014 as the brakes to the recovery are progressively being loosened. The drag from fiscal consolidation is diminishing, the financial system is slowly healing and uncertainty is decreasing. As a consequence, the International Monetary Fund (IMF) in the January update of its “World Economic Outlook” (WEO) raised its global growth projection for 2013 and 2014 by 0.1 percentage points to 3.0% and 3.7% respectively.

This projection is largely due to the recovery in the advanced economies. The IMF for example expects growth in the United States to be 2.8 percent in 2014, up from 1.9 percent in 2013 carried by domestic demand and supported in part by a reduction in the fiscal drag. In many emerging market and developing economies, stronger external demand from advanced economies will lift growth. The IMF thus expects growth in developing economies to increase from 4.7% in 2013 to 5.1% in 2014. Domestic demand however has remained weaker than expected in many emerging markets except for China. As a result, growth in 2013 or 2014 has been revised downward compared to the October 2013 forecasts, including in Brazil, Russia, the Middle East and North Africa.

The euro area meanwhile is turning the corner from recession to recovery. Growth is projected to strengthen from -0.4% in 2013 to 1.0% in 2014, but the recovery will be uneven. The pickup will generally be more modest in economies under stress, despite some upward revisions including Spain. Elsewhere in Europe, activity will be particularly buoyed in the United Kingdom where growth is expected to record 2.4 percent in 2014 driven by easier credit conditions and increased confidence.

According to Markit Economics, in August 2013 the UK construction output underwent the sharpest expansion for almost six years. The latest reading indicated a sharp rise in total business activity and the fastest pace of output expansion in the construction sector since September 2007.

UK construction companies widely reported that the latest upturn in business activity was supported by a strong improvement in spending among clients. August data signaled that incoming new work increased sharply and at the fastest rate since March 2012.

Higher levels of new business helped maintain confidence in the year-ahead outlook for construction output. August data pointed to a strong degree of positive sentiment regarding the prospects for business activity over the next 12 months.

According to Transparency Market Research, the worldwide market for physical security is expected to reach a market size of USD 125.03 billion by 2019 with a CAGR of 15% from 2013 to 2019. According to IHS research, the residential sector accounted for over 40% of the $2.7 billion global intruder alarm market in 2012, and is forecasted to grow at an annual rate of 5.3 % from 2012 to 2017. The relatively new smart home trend in North America is expected to increase the penetration rate of intruder alarm products into the residential sector. This trend is expected in Europe as well with energy-management features as one of the main drivers.

2.2 Operating and Financial Review for 2013

The financial statements of the Company as of December 31, 2013 have been prepared in accordance with the International Financial Reporting Standards (IFRS).

During the period from January 1 to December 31 of fiscal 2013 ("Reporting Period"), the Company completed the development of its new product line (ELAS, iConnect Two-way-wireless and CommPact) and put its sales focus on distributing the new product line in the market.

1) Earnings

The Company is facing internal and external challenges due to the recent developments in the global economy. These global economic developments have affected the Company's 2013 and 2012 results as well as its customers and suppliers and introduced new settings and opportunities for the future.

During the reported period, the Company implemented its business plan and fully outsourced its production activity, which had a positive effect on the Company's profitability.

US$ in thousands	12 months ended December 31, 2013	12 months ended December 31, 2012
Revenues	16,534	14,331
Gross Profit	7,027	5,324
Gross profit margin (in %)	**42%**	**37%**
Research and development	1,235	1,247
Selling and marketing	1,851	1,556
General and administrative	2,146	1,678
Other income	-	402
Financial Exp (Income), net	(37)	166
Tax income.	(1,095)	-
Net Income	**2,927**	**1,079**

The Company's revenues in the Reporting Period amounted to US$ 16.5 million, a significant rise of around 15% compared to revenues of US$ 14.3 million during the 12 month ended at December 31, 2012.

The increase in revenues is a result of the successful implementation of the Company's strategy to expand markets, recruit new customers and to find new opportunities.

The cost of goods sold amounted to US$ 9.5 million (58%) compared to US$ 9.0 million (63%) in the comparable year.

The gross profit for the Reporting Period therefore amounted to US$ 7.0 million (42% of the revenues) compared to US$ 5.3 million (37% of the revenues) in 2012. The margin increase resulted from efficiency gains, the use of outsourcing partners and continuing sales of high margin products.

Research and development expenses amounted to US$ 1.2 million during the Reporting Period, roughly the same as in the comparable year 2012.

Selling and marketing expenses increased to US$ 1.9 million during the Reporting Period, compared to US$ 1.6 million for the comparable period of last year as the Company continued to develop and expand its marketing and sales capabilities with a focus on strategic customers, while at the same time, providing more marketing and technical support to existing customers.

The general and administrative expenses amounted to US$ 2.1 million during the Reporting Period, compared to US$ 1.7 million in the comparable year.

Starting in August 2010, the Company employs management service agreements with Risco Ltd. in order to assist it in the following fields: (i) sales administration services; (ii) IT and computerized systems; (iii) finance management and accounting; (iv) human resources; (v) directors and consulting services; (vi) legal and company secretarial services.

On August 29, 2013, the Company's shareholders approved an amendment to the Management services agreement with Risco. The revised agreement includes; (i) additional services which will be rendered by Risco to the Company and (ii) revises the annual amount payable to Risco so that the base amount will be an amount of $800 instead of $300, and (iii) the agreement has been extended for an additional three years period.

The Company had no other income in the Reporting Period, while other income amounted to US$ 402,000 from the reversal of provisions in the comparable period of last year.

Going along with the rise in sales, total operating expenses for the Reporting Period also increased, to US$ 5.2 million, compared to US$ 4.1 million in the comparable year 2012.
The increase in operating expenses is mainly due the growing marketing activity and the implantation of the management service agreement between Risco and the Company as mentioned above.

Net financing expenses amounted to an income of US$ 37,000 in the Reporting Period. Financial expenses of US$ 130,000 therefore were more than offset by financial income in the amount of US$ 167,000 resulting from beneficial changes in the currency exchange rate.

Tax income in total amount of US$ 1.1 million was recorded in the reporting Period, principally due to tax loss carry forwards. The deferred tax assets were recorded based on the Company's management best estimation of realization of these losses and temporary differences in the foreseeable future.

The net profit for the Reporting Period amounted to US$ 2.9 million, compared to a net profit of US$ 1.1 million in the comparable year.

2) The Company's Financial Position

The Company's cash and cash equivalents as of December 31, 2013 (hereinafter: "the Reporting Date") increased to US$ 2.0 million, compared to US$ 0.8 million on December 31, 2012.

The Company's trade receivables on the Reporting Date amounted to US$ 0.9 million, compared to US$ 0.7 million on December 31, 2012.

The Company's prepaid expenses, other accounts receivables, advance payments to suppliers and income tax receivables on the Reporting Date amounted to US$ 0.2 million, the same as at December 31, 2012.

The Company's inventories on the Reporting Date slightly decreased to US$ 3.9 million compared to US$ 4.0 million on December 31, 2012.

Net investment in property, plant and equipment, in the Reporting Period amounted to US$ 0.6 million, the same as in the comparable period 2012.

The short term credit balance from banks on the Reporting Date amounted to US$ 0.2 million, compared to US$ 0.3 million on December 31, 2012.

The Company's trade payables as of the Reporting Date were US$ 1.7 million compared to US$ 2.0 million on December 31, 2012.

Other current liabilities, accrued expenses and income tax payable decreased to US$ 0.6 million at the Reporting Date, compared to US$ 0.8 million as at December 31, 2012.

The company had no long term loans on the Reporting Date compared to US$ 0.2 million on December 31, 2012.

Financial Ratios	December 31, 2013	December 31, 2012
Current Ratio	2.8	1.8
Quick Ratio	1.3	0.5

As of the Reporting Date, the Company complies with any bank covenants.

The Company improved its equity as of the Reporting Date to US$ 6.7 million, corresponding in an equity ratio of 71%, compared to US$ 3.7 million (52%) as of December 31, 2012.

3) Cash Flow

During the Reporting Period, net cash provided by operating activities improved to US$ 1.7 million compared to US$ 617,000 during the comparable year.

During the Reporting Period, net cash used in investing activities amounted to US$ 156,000 compared to US$ 260,000 in fiscal 2012.

During the Reporting Period, cash used in financing activities decreased to US$ 352,000, compared to US$ 1.2 million during the fiscal year 2012.

4) Employees

The number of employees remains 34, unchanged from December 31, 2012.

3. Events after the end of the reporting period

Following the Board's resolution, dated April 8, 2014, the Company's shares will be traded in the General Standard segment of the Frankfurt Stock Exchange instead of the Prime standard. This change is expected to take effect on June 30, 2014.

4. Risks and Opportunities

Risks related to the Company

Dependence on Sub-contractors

The Company depends on sub-contractors in production and in research and development services. In the event that the relationship with any of the sub-contractors is terminated, the Company may incur a delay in developing new products and in producing and supplying its products until such time as the Company is able to locate and establish a relationship with alternative sub-contractor(s) or alternatively, perform such work in-house. Additional time would be needed before such new sub-contractor(s) or internal personnel could render effective development services and prepare production files previously provided by the original sub-contractor(s). This time delay could affect the Company's ability to producing products, launch new products or introduce new versions of products in a timely manner which could adversely affect the Company's market share. In addition, any arrangement with a new sub-contractor or a decision to perform any such work in-house may increase the Company's costs and affect its gross margins.

Dependence on Integrators, Service Providers, Distributors and Installers of Systems

Currently, the Company does not typically sell its solutions to end users. The Company's traditional customers are integrators, service providers, distributors and installers of systems. Therefore, the Company is dependent, and has little control over, the customers who are, in fact, third-party installers of the Company's products. The Company has virtually no contact with end users of the product. The customers are responsible for the most part, for the sale, installation and technical support of the Company's products in relations to the end user. Due to this extended channel of distribution, the business results of the Company could be significantly harmed through changes in the business conditions of the customers which are beyond the ability of the Company to control. Installation and/or service problems could arise that might affect the sale of products to end users and because the Company does not perform the installation or service of its products at the end user facility, it might be difficult for the Company to positively impact or resolve such issues between the customer and the end user. Furthermore, the Company may not be able to preserve its current relationships or to develop new relationships with different customers. Any such change in its relationships with customers is liable to significantly harm the business affairs of the Company, affect the Company's sales, its financial condition and business results.

Dependence on Key Customers

The Company's sales to its largest four customers accounted (excluding sales to related parties) for approximately 48% of total revenues during the year 2013 (2012: approximately 45%). The Company does not have long-term purchase contracts with its customers, and sales arrangements with some of these customers do not have minimum purchase requirements. The Company cannot assure that these major customers or any other customers will continue to purchase its products at all or in the same volumes or on the same terms as they have in the past. Their failure to do so may significantly reduce the Company's revenues.

Changes in Exchange Rates

The Company is exposed to exchange rate fluctuations between the US$ and other currencies, which may negatively affect its earnings. A substantial majority of the Company's revenues are denominated in US$; however, a significant portion of the expenses associated with the Company's Israeli operations, including personnel, are incurred in NIS. The Company cannot predict any future trends in the exchange rates of the NIS against the US$. In addition, exchange rate fluctuations in currency exchange rates in countries other than Israel where the Company operates may also negatively affect the Company's earnings. These currencies currently include the Euro and the British Pound.

The Company has established certain hedging policies to protect itself against the impact of currency fluctuations going forward.

Intellectual Property

Critical to the Company's future is the Company's ability to protect its proprietary technology. The Company relies on a combination of patent, copyright, trademark and trade secret laws in order to protect its intellectual property rights.

The process of seeking patent protection can be long, expensive and sometimes unsuccessful. Therefore, the Company has chosen to file for protection of its intellectual property in certain selected markets, although not in all markets in which the Company sells its products. There can be no assurance that the Company's pending or future patent applications will result in patents being issued or that the Company's existing patents or any future patents which may be granted will provide meaningful protection or commercial advantages to the Company. A patent only provides partial protection to intellectual property, as much depends on the climate of enforcement within the country granting the patent. In addition, any issued patent may be challenged, invalidated or legally (or illegally) circumvented by third parties, and the Company cannot be certain that its patents will be upheld as valid, be enforceable or prevent the development of competitive products. Moreover, the Company sells and markets its products in some countries; e.g., China, with potentially weak enforcement of intellectual property rights. If competitors are able to develop, manufacture and sell products that directly compete with the Company's products, the Company's sales and gross margins could be adversely affected.

In addition, competitors could purchase one of the Company's systems and attempt to replicate some or all of the competitive advantages the Company derives from its development efforts or design a product based on the Company's protected proprietary technology or develop their own competitive technologies that fall outside of the Company's protected intellectual property rights. If the Company's intellectual property is not adequately protected against use by competitors and other third parties, its competitive position could be eroded and its business could be adversely affected.

Risks Pertaining to Product Liability and Product Warranty

The products developed by the Company may contain latent defects that may only be discovered after the products have been installed and are in use. Such defects could cause a reduction in customers' satisfaction, harm the reputation of the Company or create a need to introduce costly changes to the product. In addition, the Company could be exposed to potential product liability claims. This could involve significant costs to the Company. Although the Company has a Corporate General Liability insurance policy, this policy does not cover costs the Company may incur to change the product, and there is no guarantee that the Company's insurance policy will fully cover any and all types of claims pertaining to product liability or afford coverage to the full extent of such claims that may be filed against the Company.

The Company provides a limited product warranty for the use and operation of its products, many of which also contain components manufactured by third parties. In effect, the Company is warranting components which it does not manufacture. This could give rise to a situation whereby the Company provides a more extensive warranty on these third party components than the Company receives from such third party manufacturers, thus creating some warranty exposure for the Company, however the exposure of this risk is immaterial.

Marketing and Product Risk

The Company spends significant time and money to understand the needs of the market; however, the Company may misjudge market needs. The Company may design products and solutions that do not meet market demands or are not priced correctly or are not delivered to the market in a timely manner. For example, the Company may develop complementary products for its security solution with remote management capabilities which the market deems not to be necessary. If this happens, the Company's costs would increase without a corresponding increase in revenues. This may have a negative impact on the Company's operations and its financial condition.

International Markets

The Company sells its products globally, primarily in Northern & Western Europe, Latin America and Asia. As a result of operating internationally, the Company may face the following risks due to its international operations, any one of which may affect sales or the Company's profitability:

- Changes in governmental requirements and regulations and differences in various countries' requirements;
- Difficulty in collecting accounts receivables;
- Differences in customs in each country;
- Differences in taxation in different countries;
- Political and/or economic instability;
- Disruption in trade caused by civil disturbances and/or war;

- Local labor strikes that affect the Company's ability to sell or deliver products in a particular country; and
- Weakening economies in target markets.

Risks Related to the industry

Changes in Raw Material Prices

The raw materials of the Company (mainly electronic, metal and plastic components) are purchased from various suppliers throughout the world. The capacity, supply and demand for such raw materials is subject to cyclical forces and market factors as well and may fluctuate significantly and as a result, the Company may have limited ability to control its subcontractor's costs in securing raw materials that would affect directly on its own costs for finished goods. In addition, prices of raw materials may be subject to fluctuation. The Company cannot assure that it will be able to pass on to customers the increased costs associated with the procurement of raw materials. To the extent that increases in costs of raw materials cannot be passed on to customers or there is a delay in passing on the increased costs to customers, the Company is likely to absorb the increase in the cost of raw materials which may materially reduce its margin of profitability.

Delay or Discontinuation in the Supply of Finished products

Currently, the Company receives sales forecasts from the majority of its customers. Based on these sales forecasts and incoming orders, the Company purchases finished goods from it subcontractors needed for sale. The Company generally maintains a sufficient inventory of long lead-time items in order to meet its sales forecasts schedule.

The Company may choose to maintain inventories of products that exceed what is necessary for the short term in order to have a small buffer stock to compensate for shortages or cessation in the supply of components. In such an event, the Company will incur additional costs to maintain this excess inventory, which could affect its gross margins as well as its operational expenses and cash flow.

Competition and Pressure to Develop New Products

The Company operates in a competitive market environment. Competition, whether direct or indirect, may adversely affect the income and profits of the Company through pressure exerted on prices, the loss of market share or other factors. Some of the Company's current and potential competitors are large companies or conglomerates that have vast resources (including capabilities in the fields of finance, technology, production, marketing and distribution), including, for example, UTC , Tyco, Bosch and Honeywell.

In addition, new competitors, such as service providers, utility companies, cable companies, and non-security distributors, may enter into the competitive market in which the Company operates.

The Company's products deal with evolving technology. The Company must continually invest in product development in order to stay on the cutting edge of technology in its market and secure its market position. The Company's sales may be affected by newer technologies offered by competitors that are not available from the Company.

Risks Related to Israel

Security, Political and Economic Instability in Israel

The principal offices of the Company are located in Israel. Accordingly, security, political and economic conditions in Israel may directly affect the Company's business. Over the past several decades, a number of armed conflicts have occurred between Israel and its Arab neighbors. Any hostilities involving Israel or the interruption or curtailment of trade between Israel and its present trading partners could adversely affect the Company's operations. However, the ongoing hostilities and violence, future armed conflicts, political developments in other countries in the region or continued or increased terrorism, could disrupt the Company's operations or make conducting the Company's operations in Israel more difficult. Any of these factors could have the effect of increasing the Company's costs, adversely affecting the Company's financial results and the expansion of the Company's business and delaying deliveries to Customers.

Furthermore, several countries continue to restrict business with Israel, in general, and with Israeli companies, in particular, and this may limit the Company's ability to make sales to these countries. These boycotts and embargos may have an adverse impact on the operations, financial condition or the further expansion of the Company's business.

5. Outlook

Looking ahead to the business year, the Company expects an increase in revenues of 10% to approximately US$ 18 million, mainly from its strategic customers and markets, in particular, Northern and Western Europe, and from the new product lines (ELAS, iConnect 2 way and CommPact). With the increasing revenue, the Company also anticipates a continued improvement of its earnings.

The Company launched a pilot of its cloud-based solution, www.MyELAS.com, among a small group of customers, enabling them to independently register their wireless alarm systems to the cloud and thereby monitor and control their premises as well as receiving images from the motion detector cameras. In addition, customers can manage their installer base via the web admin application.

The Company expects that these new Smartphone applications for iPhone and Android, will help increase sales of the iConnect and CommPact panels.

The Company continues focusing on its Two-way-wireless iConnect product line and its PIR camera detector with a built-in camera for video verification, in addition to the release of new complimentary products such as the two-way repeater for extending the detectors' range and the two-way vibration detector, all sustaining market expansions and increased sales.

6. Responsibility Statement

"To the best of our knowledge and in accordance with the applicable reporting principles for financial reporting, the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company, and the management report of the Company includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal opportunities and risks associated with the expected development of the Company for the remaining months of the financial year."

___________________	___________________
Douglas Luscombe	Moshe Alkelai
CEO	Chairman of the Board

Rishon Le Zion, April 8, 2014

ELECTRONICS LINE 3000 LTD.

FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2013

U.S. DOLLARS IN THOUSANDS

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of

ELECTRONICS LINE 3000 LTD.

We have audited the accompanying financial statements of Electronics Line 3000 Ltd. ("the Company"), which comprise the statements of financial position as of December 31, 2013 and 2012, and the income statements, statements of comprehensive income, statements of changes in equity and statements of cash flows for each of the two years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2013 and 2012, and its financial performance and cash flows for each of the two years then ended, in accordance with International Financial Reporting Standards.

Tel-Aviv, Israel
April 8 , 2014

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ELECTRONICS LINE 3000 LTD.

STATEMENTS OF FINANCIAL POSITION

U.S. dollars in thousands

	Note	December 31, 2013	December 31, 2012
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents	5	1,988	803
Trade receivables	6	927	658
Other accounts receivable	7	164	170
Inventories	8	3,912	4,042
Total current assets		6,991	5,673
NON-CURRENT ASSETS:			
Property, plant and equipment, net	9	574	609
Intangible assets	10	202	303
Deferred taxes	16e	1,593	498
Security deposits		34	17
Total non-current assets		2,403	1,427
Total assets		9,394	7,100

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

ELECTRONICS LINE 3000 LTD.

STATEMENTS OF FINANCIAL POSITION

U.S. dollars in thousands

	Note	December 31, 2013	December 31, 2012
LIABILITIES AND EQUITY			
CURRENT LIABILITIES:			
Short-term credit from banks	11	179	351
Trade payables	12	1,728	1,956
Other current liabilities	13	563	811
Total current liabilities		2,470	3,118
NON-CURRENT LIABILITIES:			
Loans from banks	14	-	179
Employee benefit liabilities, net	15	240	143
Total non-current liabilities		240	322
EQUITY:	18		
Share capital		15,933	15,933
Additional paid-in capital		6,632	6,584
Accumulated deficit		(15,881)	(18,857)
Total equity		6,684	3,660
Total liabilities and equity		9,394	7,100

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

April 8 , 2014			
Date of approval of the financial statements	Moshe Alkelai Chairman of the Board	Douglas Luscombe President and CEO	Sharon Sheep Responsible for finance

ELECTRONICS LINE 3000 LTD.

INCOME STATEMENTS

U.S. dollars in thousands, except per share data

	Note	Year ended December 31, 2013	2012
Revenues	20	16,534	14,331
Cost of revenues	21	9,507	*) 9,007
Gross profit		7,027	5,324
Operating costs and expenses:			
Research and development	22	1,235	*) 1,247
Selling and marketing	23	1,851	1,556
General and administrative	24	2,146	1,678
Other expenses (income), net	25	-	(402)
Total operating costs and expenses		5,232	4,079
Operating income		1,795	1,245
Financial income	26a	167	-
Financial expenses	26b	130	166
Income before taxes on income		1,832	1,079
Income tax benefit	16b	1,095	-
Net income		2,927	1,079
Net income per share (basic and diluted)	27	0.21	0.08

*) Reclassified, see Note 2r.

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

ELECTRONICS LINE 3000 LTD.

STATEMENTS OF COMPREHENSIVE INCOME

U.S. dollars in thousands

	Year ended December 31, 2013	Year ended December 31, 2012
Net income	2,927	1,079
Other comprehensive income:		
Amounts that will not be reclassified subsequently to profit or loss:		
Remeasurement gain from defined benefit plans	49	-
Total other comprehensive income	49	-
Total comprehensive income	2,976	1,079

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

ELECTRONICS LINE 3000 LTD.

STATEMENTS OF CHANGES IN EQUITY

U.S. dollars in thousands

	Share capital	Additional paid-in capital	Accumulated deficit	Total equity
Balance as of January 1, 2012	15,933	6,474	(19,936)	2,471
Total comprehensive income	-	-	1,079	1,079
Cost of share-based payments		110		110
Balance as of December 31, 2012	15,933	6,584	(18,857)	3,660
Net income	-	-	2,927	2,927
Other comprehensive income	-	-	49	49
Total comprehensive income	-	-	2,976	2,976
Cost of share-based payments	-	48	-	48
Balance as of December 31, 2013	15,933	6,632	(15,881)	6,684

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

ELECTRONICS LINE 3000 LTD.

STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31, 2013	Year ended December 31, 2012
Cash flows from operating activities:		
Net income	2,927	1,079
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Adjustments to profit or loss items:		
Depreciation and amortization	292	273
Loss from sale of property, plant and equipment	-	2
Increase in employee benefit liabilities, net	146	3
Cost of share-based payments	48	110
Income tax benefit	(1,095)	-
Financial expenses, net	129	128
	(480)	516
Changes in operating asset and liability items:		
Decrease (increase) in trade receivables	(269)	1,359
Decrease in other accounts receivable	9	1,735
Decrease (increase) in inventories	130	(2,619)
Decrease (increase) in security deposits	(17)	63
Decrease in trade payables	(228)	(840)
Decrease in other long-term liabilities	-	(426)
Decrease in other current liabilities	(248)	(114)
	(623)	(842)
Interest paid	(129)	(128)
Income taxes paid	(3)	(8)
	(132)	(136)
Net cash provided by operating activities	1,692	617
Cash flows from investing activities:		
Purchase of property, plant and equipment	(156)	(274)
Proceeds from sale of equipment	-	14
Net cash used in investing activities	(156)	(260)

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

ELECTRONICS LINE 3000 LTD.

STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,	
	2013	**2012**
Cash flows from financing activities:		
Repayment of long-term loans from banks	(351)	(1,241)
Net cash used in financing activities	(351)	(1,241)
Increase (decrease) in cash and cash equivalents	1,185	(884)
Cash and cash equivalents at beginning of year	803	1,687
Cash and cash equivalents at end of year	1,988	803

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

NOTE 1:- GENERAL

a. Electronics Line 3000 Ltd. ("the Company") was incorporated in Israel in December 2002.

The Company's shares are publicly traded on the Prime Standard, a market operated by the Frankfurt Stock Exchange.

Following the Board's resolution, dated April 8, 2014 the Company changed the trading of its shares from the Prime Standard to the General Standard segment of the Frankfurt Stock Exchange. The Company's transfer to trading in the General Standard segment will take effect on June 30, 2014.

b. The Company is engaged in the design, development, production, marketing and sale of electronic security with remote management solutions, and complementary products for the mass residential and small commercial markets. These solutions can be monitored and enable remote management of the premises for security, and automation and video application. The registered office of the Company is located at 14 Hachoma Street, Rishon LeZion, Israel

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES

The following accounting policies have been applied consistently in the financial statements for all periods presented, unless otherwise stated.

a. Basis of presentation of the financial statements:

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").
The Company's financial statements have been prepared on a cost basis, except for: financial assets and liabilities (including derivatives) which are presented at fair value through profit or loss.

The Company has elected to present profit or loss items using the function of expense method.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The preparation of the financial statements requires management to make critical accounting estimates as well as exercise judgment in the process of adopting significant accounting policies. The matters which required the exercise of significant judgment and the use of estimates, which have a material effect on amounts recognized in the financial statements, are specified in Note 3 below.

b. Functional currency, presentation currency and foreign currency:

1. Functional currency and presentation currency:

The presentation and the functional currency of the financial statements is the U.S. dollar.

2. Transactions, assets and liabilities in foreign currency:

Transactions denominated in foreign currency are recorded upon initial recognition at the exchange rate at the date of the transaction. After initial recognition, monetary assets and liabilities denominated in foreign currency are translated at each reporting date into the functional currency at the exchange rate at that date. Exchange rate differences, other than those capitalized to qualifying assets, are recognized in profit or loss. Non-monetary assets and liabilities denominated in foreign currency and measured at cost are translated at the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currency and measured at fair value are translated into the functional currency using the exchange rate prevailing at the date when the fair value was determined.

d. Cash equivalents:

Cash equivalents are considered as highly liquid investments, including unrestricted short-term bank deposits with an original maturity of three months or less from the date of acquisition.

e. Allowance for doubtful accounts:

The allowance for doubtful accounts is determined in respect of specific debts whose collection, in the opinion of the Company's management, is doubtful. Impaired debts are derecognized when they are assessed as uncollectible.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

g. Inventories:

Inventories are measured at the lower of cost and net realizable value. The cost of inventories comprises costs of purchase and costs incurred in bringing the inventories to their present location and condition. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated selling costs. The Company periodically evaluates the condition and age of inventories and makes provisions for slow moving inventories accordingly.

Cost of inventories is determined as follows:

Purchased products and raw materials - using the weighted average cost method.

h. Revenue recognition:

Revenues are recognized in profit or loss when the revenues can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Company and the costs incurred or to be incurred in respect of the transaction can be measured reliably. In cases where the Company acts as an agent or as a broker without being exposed to the risks and rewards associated with the transaction, its revenues are presented on a net basis. Revenues are measured at the fair value of the consideration received less any trade discounts, volume rebates and returns.

Following are the specific revenue recognition criteria which must be met before revenue is recognized:

Revenues from the sale of goods:

Revenues from the sale of goods are recognized when all the significant risks and rewards of ownership of the goods have passed to the buyer and the seller no longer retains continuing managerial involvement. The delivery date is usually the date on which ownership passes.

Revenues from "bill and hold" sales are recognized before delivery provided that:

1. it is probable that delivery will be made;
2. the item is on hand, identified and ready for delivery to the buyer at the time the sale is recognized;
3. the buyer specifically acknowledges, preferably in writing, the deferred delivery instructions;
4. the delivery instructions as stated in 3 above specify a fixed delivery date that is reasonable and consistent with the buyer's business objectives; and
5. the usual payment terms apply.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Customer discounts:

Customer discounts given at the end of the year and in respect of which the customer is not obligated to comply with certain targets, are recognized in the financial statements proportionately as the sales entitling the customer to said discounts are made.

Customer discounts for which the customer is required to meet certain targets, such as a minimum amount of annual purchases (either quantitative or monetary), an increase in purchases compared to previous periods, etc. are recognized in the financial statements in proportion to the purchases made by the customer during the year that qualify for the target, provided that it is expected that the targets will be achieved and the amount of the discount can be reasonably estimated.

i. Taxes on income:

Taxes on income in profit or loss comprise current and deferred taxes. Current or deferred taxes are recognized in profit or loss, except to the extent that the tax arises from items which are recognized directly in other comprehensive income or in equity. In such cases, the tax effect is also recognized in the relevant item.

1. Current taxes:

   The current tax liability is measured using the tax rates and tax laws that have been enacted or substantively enacted by the end of reporting period as well as adjustments required in connection with the tax liability in respect of previous years.

2. Deferred taxes:

   Deferred taxes are computed in respect of temporary differences between the carrying amounts in the financial statements and the amounts attributed for tax purposes.

   Deferred taxes are measured at the tax rates that are expected to apply when the asset is realized or the liability is settled, based on tax laws that have been enacted or substantively enacted by the end of the reporting period. Deferred taxes in profit or loss represent the changes in the carrying amount of deferred tax balances during the reporting period, excluding changes attributable to items recognized in other comprehensive income or in equity.

   Deferred tax assets are reviewed at the end of each reporting period and reduced to the extent that it is not probable that they will be utilized. Temporary differences (such as carryforward losses) for which deferred tax assets had not been recognized are reviewed at the end of each reporting period and a respective deferred tax asset is recognized to the extent that their utilization is probable.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

All deferred tax assets and deferred tax liabilities are presented in the statement of financial position as non-current assets and non-current liabilities, respectively.

j. Property, plant and equipment:

Property, plant and equipment are measured at cost, including directly attributable costs, less accumulated depreciation, accumulated impairment losses and any related investment grants and excluding day-to-day servicing expenses. Cost includes spare parts and auxiliary equipment that are used in connection with plant and equipment.

A part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item is depreciated separately.

Depreciation is calculated on a straight-line basis over the useful life of the assets at annual rates as follows:

	%	Mainly %
Machinery and equipment	10 - 15	10
Motor vehicles	15	15
Office furniture and equipment	6 - 33	33

The useful life, depreciation method and residual value of an asset are reviewed at least each year-end and any changes are accounted for prospectively as a change in accounting estimate.

Depreciation of an asset ceases at the earlier of the date that the asset is classified as held for sale and the date that the asset is derecognized. An asset is derecognized on disposal or when no further economic benefits are expected from its use. The gain or loss arising from the derecognition of the asset (determined as the difference between the net disposal proceeds and the carrying amount in the financial statements) is included in profit or loss when the asset is derecognized.

k. Intangible assets:

Expenditures relating to internally generated intangible assets, excluding capitalized development costs, are recognized in profit or loss when incurred. After initial recognition, intangible assets are carried at their cost less any accumulated amortization and any accumulated impairment losses.

Intangible assets with a finite useful life are amortized over their useful life and reviewed for impairment whenever there is an indication that the asset may be impaired. The amortization period and the amortization method for an intangible asset are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for prospectively as changes in accounting estimates. The amortization of intangible assets with finite useful lives is recognized in profit or loss.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Gains or losses arising from the derecognition of an intangible asset are determined as the difference between the net disposal proceeds and the carrying amount of the asset and are recognized in profit or loss.

The useful life of intangible assets is as follows:

	Years
Product files	5

Research and development expenditures:

Research expenditures are recognized in profit or loss when incurred. An intangible asset arising from a development project or from the development phase of an internal project is recognized if the Company can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale; the Company's intention to complete the intangible asset and use or sell it; the Company's ability to use or sell the intangible asset; how the intangible asset will generate future economic benefits; the availability of adequate technical, financial and other resources to complete the intangible asset; and the Company's ability to measure reliably the expenditure attributable to the intangible asset during its development.

The asset is measured at cost less any accumulated amortization and any accumulated impairment losses. Amortization of the asset begins when development is complete and the asset is available for use. The asset is amortized over its useful life. Testing of impairment is performed annually over the period of the development project.

l. Impairment of non-financial assets:

The Company evaluates the need to record an impairment of the carrying amount of non-financial assets whenever events or changes in circumstances indicate that the carrying amount is not recoverable. If the carrying amount of non-financial assets exceeds their recoverable amount, the assets are reduced to their recoverable amount. The recoverable amount is the higher of fair value less costs of sale and value in use. In measuring value in use, the expected future cash flows are discounted using a pre-tax discount rate that reflects the risks specific to the asset. The recoverable amount of an asset that does not generate independent cash flows is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognized in profit or loss.

An impairment loss of an asset, other than goodwill, is reversed only if there have been changes in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. Reversal of an impairment loss, as above, shall not be increased above the lower of the carrying amount that would have been determined (net of depreciation or amortization) had no impairment loss been recognized for the asset in prior years, and its recoverable amount. The reversal of impairment loss of an asset presented at cost is recognized in profit or loss.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The following criteria are applied in assessing impairment of these specific assets:

Development costs capitalized during the development period:

The impairment test is performed annually, on December 31, or more frequently if events or changes in circumstances indicate that there is an impairment

m. Financial instruments:

1. Financial assets:

Financial assets within the scope of IAS 39 are initially recognized at fair value plus directly attributable transaction costs, except for financial assets measured at fair value through profit or loss in respect of which transaction costs are recorded in profit or loss.
After initial recognition, the accounting treatment of financial assets is based on their classification as follows:

a) Financial assets at fair value through profit or loss:

This category includes financial assets held for trading (including derivatives) and financial assets designated upon initial recognition as at fair value through profit or loss.

Embedded derivatives are separated from the host contract and accounted for separately if: (a) the economic characteristics and risks of the embedded derivatives are not closely related to those of the host contract; (b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and (c) the combined instrument is not measured at fair value through profit or loss.

b) Loans and receivables:

Loans and receivables are investments with fixed or determinable payments that are not quoted in an active market. After initial recognition, loans are measured based on their terms at amortized cost less directly attributable transaction costs using the effective interest method and less any impairment losses. Short-term receivables are measured based on their terms, normally at face value.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

2. Financial liabilities:

Financial liabilities within the scope of IAS 39 are classified as either financial liabilities at fair value through profit or loss, loans at amortized cost or derivatives designated as effective hedging instruments. The Company determines the classification of the liability on the date of initial recognition. All liabilities are initially recognized at fair value. Loans are presented net of directly attributable transaction costs.

After initial recognition, the accounting treatment of financial liabilities is based on their classification as follows:

a) Financial liabilities at amortized cost:

After initial recognition, loans, including debentures, are measured based on their terms at amortized cost less directly attributable transaction costs using the effective interest method. The amortization of the effective interest is recognized in profit or loss in the line item, "financing".

b) Financial liabilities at fair value through profit or loss:

Financial liabilities at fair value through profit or loss include financial liabilities classified as held for trading (including derivatives) and financial liabilities designated upon initial recognition as at fair value through profit or loss.

3. Derecognition of financial instruments:

a) Financial assets:

A financial asset is derecognized when the contractual rights to the cash flows from the financial asset expire or the Company has transferred its contractual rights to receive cash flows from the financial asset or assumes an obligation to pay the cash flows in full without material delay to a third party and has transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A transaction involving factoring of accounts receivable is derecognized when the abovementioned conditions are met.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

If the Company transfers its rights to receive cash flows from an asset and neither transfers nor retains substantially all the risks and rewards of the asset nor transfers control of the asset, a new asset is recognized to the extent of the Company's continuing involvement in the asset. When continuing involvement takes the form of guaranteeing the transferred asset, the extent of the continuing involvement is the lower of the original carrying amount of the asset and the maximum amount of consideration received that the Company could be required to repay.

b) Financial liabilities:

A financial liability is derecognized when it is extinguished, that is when the obligation is discharged or cancelled or expires. A financial liability is extinguished when the debtor (the Company) discharges the liability by paying in cash, other financial assets, goods or services; or is legally released from the liability.

4. Impairment of financial assets:

The Company assesses at the end of each reporting period whether there is any objective evidence of impairment of a financial asset or group of financial assets as follows.

Financial assets carried at amortized cost:

Objective evidence of impairment exists when one or more events that have occurred after the initial recognition of the asset have a negative impact on the estimated future cash flows. Evidence of impairment may include indications that the debtor is experiencing financial difficulties, including liquidity difficulty and default in interest or principal payments. The amount of the loss recorded in profit or loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not yet been incurred) discounted at the financial asset's original effective interest rate (the effective interest rate computed at initial recognition). If the financial asset has a variable interest rate, the discount rate is the current effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account (see allowance for doubtful accounts above). In a subsequent period, the amount of the impairment loss is reversed if the recovery of the asset can be related objectively to an event occurring after the impairment was recognized. The amount of the reversal, up to the amount of any previous impairment, is recorded in profit or loss.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

n. Provisions:

A provision in accordance with IAS 37 is recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. If the Company expects part or all of the expense to be reimbursed to the Company, such as in an insurance contract, the reimbursement is recognized as a separate asset only when it is virtually certain that it will be received by the Company. The expense is recognized in the income statement net of the reimbursed amount.

Following are the types of provisions included in the financial statements:

Legal claims:

A provision for claims is recognized when the Company has a present legal or constructive obligation as a result of a past event, it is more likely than not that an outflow of resources embodying economic benefits will be required by the Company to settle the obligation and a reliable estimate can be made of the amount of the obligation.

o. Employee benefit liabilities:

The Company has several employee benefit plans:

1. Short-term employee benefits:

Short-term employee benefits are benefits that are expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related services. These benefits include salaries, paid annual leave, paid sick leave, recreation and social security contributions and are recognized as expenses as the services are rendered. A liability in respect of a cash bonus or a profit-sharing plan is recognized when the Group has a legal or constructive obligation to make such payment as a result of past service rendered by an employee and a reliable estimate of the amount can be made.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

2. Post-employment benefits:

The plans are normally financed by contributions to insurance companies and classified as defined contribution plans or as defined benefit plans.

The Company has defined contribution plans pursuant to Section 14 to the Severance Pay Law under which the Company pays fixed contributions and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient amounts to pay all employee benefits relating to employee service in the current and prior periods. Contributions to the defined contribution plan in respect of severance or retirement pay are recognized as an expense when contributed concurrently with performance of the employee's services.

The Company also operates a defined benefit plan in respect of severance pay pursuant to the Severance Pay Law. According to the Law, employees are entitled to severance pay upon dismissal or retirement. The liability for termination of employment is measured using the projected unit credit method. The actuarial assumptions include expected salary increases and rates of employee turnover based on the estimated timing of payment. The amounts are presented based on discounted expected future cash flows using a discount rate determined by reference to yields on Government bonds with a term that is consistent with the estimated term of the severance pay obligation.

In respect of its severance pay obligation to certain of its employees, the Company makes current deposits in pension funds and insurance companies ("the plan assets"). Plan assets comprise assets held by a long-term employee benefit fund or qualifying insurance policies. Plan assets are not available to the Company's own creditors and cannot be returned directly to the Company.

The liability for employee benefits shown in the statement of financial position reflects the present value of the defined benefit obligation less the fair value of the plan assets.

Remeasurements of the net liability are recognized in other comprehensive income in the period in which they occur.

p. Share-based payment transactions:

The Company's employees, other employees of the parent company and the Company’s directors are entitled to remuneration in the form of equity-settled share-based payment transactions.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Equity-settled transactions:

The cost of equity-settled transactions with employees, employees of the parent company and its Directors is measured at the fair value of the equity instruments granted at grant date. The fair value is determined using an acceptable option pricing model.

The cost of equity-settled transactions is recognized in profit or loss, together with a corresponding increase in equity, during the period which the performance is to be satisfied, ending on the date on which the relevant employees become fully entitled to the award ("the vesting period"). The cumulative expense recognized for equity-settled transactions at the end of each reporting period until the vesting date reflects the extent to which the vesting period has expired and the Company’s best estimate of the number of equity instruments that will ultimately vest. The expense or income recognized in profit or loss represents the change between the cumulative expense recognized at the end of the reporting period and the cumulative expense recognized at the end of the previous reporting period.
No expense is recognized for awards that do not ultimately vest.

If the Company modifies the conditions on which equity-instruments were granted, an additional expense is recognized for any modification that increases the total fair value of the share-based payment arrangement or is otherwise beneficial to the employee/ employees of the parent company at the modification date.

If a grant of an equity instrument is cancelled, it is accounted for as if it had vested on the cancellation date, and any expense not yet recognized for the grant is recognized immediately. However, if a new grant replaces the cancelled grant and is identified as a replacement grant on the grant date, the cancelled and new grants are accounted for as a modification of the original grant, as described above.

q. Earnings per share:

Earnings per share are calculated by dividing the net income attributable to equity holders of the Company by the weighted number of Ordinary shares outstanding during the period. Potential Ordinary shares (convertible securities such as convertible debentures, warrants and employee options) are only included in the computation of diluted earnings per share when their conversion decreases earnings per share or increases loss per share from continuing operations. Potential Ordinary shares that are converted during the period are included in diluted earnings per share only until the conversion date and from that date in basic earnings per share.

r. Reclassification:

Amounts related to amortization of capitalized development costs previously presented in research and development expenses are now included in cost of revenues.
Comparative data were reclassified, and accordingly, $102 was reclassified from research and development expenses, to cost of revenues for the year ended December 31, 2012.

NOTE 3:- SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUPMTIONS USED IN THE PREPARATION OF THE FINANCIAL STATEMENTS

In the process of applying the significant accounting policies, the Company has made the following judgments which have the most significant effect on the amounts recognized in the financial statements:

a. Judgments:

- Determining the fair value of share-based payment transactions:

  The fair value of share-based payment transactions is determined using an acceptable option-pricing model. The model includes data as to the share price and exercise price, and assumptions regarding expected volatility, expected life, expected dividend and risk-free interest rate.

b. Estimates and assumptions:

The preparation of the financial statements requires management to make estimates and assumptions that have an effect on the application of the accounting policies and on the reported amounts of assets, liabilities, revenues and expenses. Changes in accounting estimates are reported in the period of the change in estimate.

The key assumptions made in the financial statements concerning uncertainties at the end of the reporting period and the critical estimates computed by the Company that may result in a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

- Legal claims:

  In estimating the likelihood of outcome of legal claims filed against the Company and its investees, the companies rely on the opinion of their legal counsel. These estimates are based on the legal counsel's best professional judgment, taking into account the stage of proceedings and legal precedents in respect of the different issues. Since the outcome of the claims will be determined in courts, the results could differ from these estimates.

- Deferred tax assets:

  Deferred tax assets are recognized for unused carryforward tax losses and deductible temporary differences to the extent that it is probable that taxable profit will be available against which the losses can be utilized. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

NOTE 3:- SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUPMTIONS USED IN THE PREPARATION OF THE FINANCIAL STATEMENTS (Cont.)

- Pension and other post-employment benefits:

  The liability in respect of post-employment defined benefit plans is determined using actuarial valuations. The actuarial valuation involves making assumptions about, among others, the discount rate, future salary increases and employee turnover rate. The carrying amount of the liability may be significantly affected by changes in these estimates.

- Development costs:

  In testing impairment of development costs, management makes assumptions regarding the expected cash flows from the asset being developed, the discount rate and the expected period of benefits.

NOTE 4:- DISCLOSURE OF NEW STANDARDS IN THE PERIOD PRIOR TO THEIR ADOPTION

a. Amendments to IAS 32, "Financial Instruments: Presentation regarding Offsetting Financial Assets and Financial Liabilities":
The IASB issued amendments to IAS 32 ("the amendments to IAS 32") regarding the offsetting of financial assets and financial liabilities.

The amendments to IAS 32 are to be applied retrospectively from the financial statements for annual periods beginning on January 1, 2014 or thereafter. Earlier application is permitted.

The Company believes that the amendments to IAS 32 are not expected to have a material impact on the financial statements.

b. IFRS 9 - Financial Instruments:

The IASB issued IFRS 9, "Financial Instruments", the first part of Phase 1 of a project to replace IAS 39, "Financial Instruments: Recognition and Measurement". IFRS 9 (the "Standard") focuses mainly on the classification and measurement of financial assets and it applies to all financial assets within the scope of IAS 39.

Amendments regarding derecognition and financial liabilities (Phase 2) have also been issued. According to those amendments, the provisions of IAS 39 will continue to apply to derecognition and to financial liabilities for which the fair value option (designated as measured at fair value through profit or loss) has not been elected; that is, the classification and measurement provisions of IAS 39 will continue to apply to financial liabilities held for trading and financial liabilities measured at amortized cost.

NOTE 4:- DISCLOSURE OF NEW STANDARDS IN THE PERIOD PRIOR TO THEIR ADOPTION

In November 2013, the IASB issued a new version of IFRS 9 (IFRS 9 (2013)) which includes the new hedge accounting requirements and related amendments to IFRS 9, IFRS 7 and IAS 39.

IFRS 9 (2013) does not have a mandatory effective date, but it is available for adoption now.

The Company is evaluating the possible impact of IFRS 9 but is presently unable to assess its effect, if any, on the financial statements.

c. Amendment to IAS 19 regarding the accounting for contributions linked to service:

The IASB issued an amendment to the existing requirements of IAS 19 regarding contributions made by employees or third parties that are linked to service.
The amendment to IAS 19 isto be applied retrospectively from the financial statements for annual periods beginning on January 1, 2014 or thereafter. Earlier application is permitted.

The Company believes that the amendment to IAS 19 is not expected to have a material impact on the financial statements.

d. Amendments to IAS 36, "Impairment of Assets":

In May 2013, the IASB issued amendments to IAS 36, "Impairment of Assets" ("the amendments") regarding the disclosure requirements of fair value less costs of disposal. The amendments include additional disclosure requirements of the recoverable amount and fair value. The additional disclosures include the fair value hierarchy, the valuation techniques and change therein, the discount rates and the principal assumptions underlying the valuations.

The amendments are effective for annual periods beginning on January 1, 2014 or thereafter. Earlier application is permitted.

The appropriate disclosures will be included in the Company's financial statements upon the first-time adoption of the amendments.

U.S. dollars in thousands

NOTE 5:- CASH AND CASH EQUIVALENTS

Composition by currency:

	December 31, 2013	December 31, 2012
U.S. dollars	1,469	588
Euros	380	69
GBP	12	41
NIS	127	105
	1,988	803

NOTE 6:- TRADE RECEIVABLES

a. Composition:

	December 31, 2013	December 31, 2012
Open accounts	1,029	735
Less - allowance for doubtful accounts	(102)	(77)
Trade receivables, net	927	658

Impaired debts are accounted for through recording an allowance for doubtful accounts.

Trade receivables are non-interest bearing and are generally for 60-120 day terms.

b. The movements in the allowance for doubtful accounts were as follows:

	Individually impaired
At January 1, 2012	84
Charge for the year	7
Reversal of collected doubtful accounts	(10)
Derecognition of bad debts	(4)
At December 31, 2012	77
Charge for the year	39
Derecognition of bad debts	(14)
At December 31, 2013	102

U.S. dollars in thousands

NOTE 6:- TRADE RECEIVABLES (Cont.)

c. An analysis of past due but not impaired trade receivables (allowance for doubtful accounts), trade receivables, net, with reference to reporting date:

	Neither past due nor impaired	Past due but not impaired < 30 days	30 - 60 days	60 -90 days	> 90 day	Total
December 31, 2013	242	677	1	-	7	927
December 31, 2012	220	348	23	5	62	658

NOTE 7:- OTHER ACCOUNTS RECEIVABLE

	December 31, 2013	December 31, 2012
Prepaid expenses	32	42
Advances to suppliers	-	4
Government authorities	116	96
Other receivables	16	28
	164	170

NOTE 8:- INVENTORIES

	December 31, 2013	December 31, 2012
Finished products	3,462	3,086
Raw materials	142	352
	3,704	3,438
Inventory in transit	208	604
	3,912	4,042

The write-downs recorded for slow-moving inventories in 2013 and 2012 amounted to $ 194 and $ 291, respectively.

U.S. dollars in thousands

NOTE 9:- PROPERTY, PLANT AND EQUIPMENT

a. Composition and movement:

	Installations and leasehold improvements	Machinery and equipment	Motor vehicles	Office furniture and equipment	Total
Cost:					
Balance at January 1, 2012	5,915	4,427	40	3,476	13,858
Acquisitions during the year	-	257	-	17	274
Disposals during the year	-	-	-	(54)	(54)
Assets fully depreciated and no longer in use	(5,905)	(3,736)	(40)	(146)	(9,827)
Balance at December 31, 2012	10	948	-	3,293	4,251
Acquisitions during the year	-	91	-	65	156
Balance at December 31, 2013	10	1,039	-	3,358	4,407
Accumulated depreciation:					
Balance at January 1, 2012	5,906	4,177	40	3,211	13,334
Provision during the year	1	96	-	76	173
Disposals during the year	-	-	-	(38)	(38)
Assets fully depreciated and no longer in use	(5,905)	(3,736)	(40)	(146)	(9,827)
Balance at December 31, 2012	2	537	-	3,103	3,642
Provision during the year	1	115	-	75	191
Balance at December 31, 2013	3	652	-	3,178	3,833
Depreciated cost at December 31, 2013	7	387	-	180	574
Depreciated cost at December 31, 2012	8	411	-	190	609

NOTE 10:- INTANGIBLE ASSETS

Internal development costs of production files that have been capitalized are composed as follows:

	December 31, 2013	December 31, 2012
Balance:		
As of January 1	504	504
Accumulated amortizations	(302)	(201)
As of December 31	202	303

U.S. dollars in thousands

NOTE 11:- SHORT-TERM CREDIT FROM BANKS

a. Composition:

	Annual interest rate	December 31, 2013	December 31, 2012
	%		
Current maturities of long-term loans (see note 14)	LIBOR + 3.5	179	351

b. Liens:

As of the balance sheet date the Company has floating charges (a non specific lien on all assets of the Company on which there is no previous specific lien) on its assets in favor of one of the Company's banks.

NOTE 12:- TRADE PAYABLES

	December 31, 2013	December 31, 2012
Open accounts	1,728	1,956
	1,728	1,956

Trade payables are non-interest bearing and generally have terms of 60-90 days.

NOTE 13:- OTHER CURRENT LIABILITIES

	December 31, 2013	December 31, 2012
Accrued expenses	161	155
Accrued salaries and related expenses	324	270
Others	78	386
	563	811

U.S. dollars in thousands

NOTE 14:- LOANS FROM BANKS

a. Composition:

	Average interest rate	December 31, 2013	December 31, 2012
	%		
U.S. dollars	LIBOR + 3.5 (1)	179	530
Less - current maturities		(179)	(351)
		-	179

(1) As of December 31, 2013, three-month LIBOR is 0.25% (2012 - 0.3%).

b. Banks covenants are as follows:

- Tangible equity to balance sheet ratio – at least 20%.
- Debt to EBITDA ratio - will not be more than 4 as of December 31, 2013 and will not be more than 3 as of December 31, 2014 and onwards.
- Operating profit - a positive operating profit in each four consecutive quarters.

As of December 31, 2013 the Company is meeting its bank covenants.

NOTE 15:- EMPLOYEE BENEFIT LIABILITIES, NET

Employee benefits consist of short-term benefits and post-employment benefits.

Post-employment benefits:

According to the labor laws and Severance Pay Law in Israel, the Company is required to pay compensation to an employee upon dismissal or retirement or to make current contributions in defined contribution plans pursuant to Section 14 to the Severance Pay Law, as specified below. The Company's liability is accounted for as a post-employment benefit. The computation of the Company's employee benefit liability is made in accordance with a valid employment contract based on the employee's salary and employment term which establish the entitlement to receive the compensation.

The post-employment employee benefits are normally financed by contributions classified as defined benefit plans or as defined contribution plans, as detailed below.

U.S. dollars in thousands

NOTE 15:- EMPLOYEE BENEFIT LIABILITIES, NET (Cont.)

a. Defined contribution plans:

Section 14 to the Severance Pay Law, 1963 applies to part of the compensation payments, pursuant to which the fixed contributions paid by the Company into pension funds and/or policies of insurance companies release the Company from any additional liability to employees for whom said contributions were made. These contributions and contributions for compensation represent defined contribution plans.

	Year ended December 31, 2013	2012
Expense in respect of defined contribution plans	94	81

b. Defined benefit plans:

The Company accounts for that part of the payment of compensation that is not covered by contributions in defined contribution plans, as above, as a defined benefit plan for which an employee benefit liability is recognized and for which the Company deposits amounts in central severance pay funds and in qualifying insurance policies.

1. Expenses recognized in the statement of income:

	Year ended December 31, 2013	2012
Current service cost	124	16
Interest cost on benefit obligation	26	24
Interest income on plan assets	(18)	(18)
Net actuarial loss recognized in the year	(49)	1
Total employee benefit expenses	83	23
Actual return on plan assets	27	36

2. The defined benefit liability, net:

	December 31, 2013	2012
Defined benefit obligation	566	420
Fair value of plan assets	(326)	(277)
Total liabilities, net	240	143

U.S. dollars in thousands

NOTE 15:- EMPLOYEE BENEFIT LIABILITIES, NET (Cont.)

3. Changes in the present value of defined benefit obligation:

	2013	2012
Balance at January 1,	420	419
Interest cost	26	24
Current service cost	124	16
Benefits paid	-	(66)
Net actuarial (gain) loss	(40)	19
Exchange differences	36	8
Balance at December 31,	566	420

4. Plan assets:

   a) Plan assets comprise assets held by a long-term employee benefit fund and qualifying insurance policies.

   b) The movement in the fair value of the plan assets:

	2013	2012
Balance at January 1,	277	278
Interest income	18	18
Benefits paid	-	(43)
Net actuarial gain	9	18
Exchange differences	22	6
Balance at December 31,	326	277

5. The principal actuarial assumptions used are as follows:

	December 31,	
	2013	2012
Discount rate	4%	4%
Future salary increase	3%	5%

NOTE 16:- TAXES ON INCOME

a. Tax laws applicable to the Company:

1. Income Tax (Inflationary Adjustments) Law, 1985:

According to the law, until 2007, the results for tax purposes were adjusted for the changes in the Israeli CPI.

In February 2008, the "Knesset" (Israeli parliament) passed an amendment to the Income Tax (Inflationary Adjustments) Law, 1985, which limits the scope of the law starting 2008 and thereafter. Since 2008, the results for tax purposes are measured in nominal values, excluding certain adjustments for changes in the Israeli CPI carried out in the period up to December 31, 2007. Adjustments relating to capital gains such as for sale of property (betterment) and securities continue to apply until disposal. Since 2008, the amendment to the law includes, among others, the cancellation of the inflationary additions and deductions and the additional deduction for depreciation (in respect of depreciable assets purchased after the 2007 tax year).

2. The Law for the Encouragement of Industry (Taxation), 1969:

The Company has the status of an "industrial company", as implied by this law. According to this status and by virtue of regulations published thereunder, the Company is entitled to claim a deduction of accelerated depreciation on equipment used in industrial activities, as determined in the regulations issued under the Inflationary Law.

b. Tax rates applicable to the Company

The Israeli corporate tax rate was 25% in 2012 and 2013.

A company is taxable on its real (non-inflationary) capital gains at the corporate tax rate in the year of sale. A temporary provision for 2006-2009 stipulates that the sale of an asset other than a quoted security (excluding goodwill that was not acquired) that had been purchased prior to January 1, 2003, and sold by December 31, 2009, is subject to corporate tax as follows: the part of the real capital gain that is linearly attributed to the period prior to December 31, 2002 is subject to the corporate tax rate in the year of sale as set forth in the Israeli Income Tax Ordinance, and the part of the real capital gain that is linearly attributed to the period from January 1, 2003, through December 31, 2009, is subject to tax at a rate of 25%.

U.S. dollars in thousands

NOTE 16:- TAXES ON INCOME (Cont.)

On December 5, 2011, the Israeli Parliament (the Knesset) passed the Law for Tax Burden Reform (Legislative Amendments), 2011 ("the Law") which, among others, cancels effective from 2012, the scheduled progressive reduction in the corporate tax rate. The Law also increases the corporate tax rate to 25% in 2012. In view of this increase in the corporate tax rate to 25% in 2012, the real capital gains tax rate and the real betterment tax rate were also increased accordingly.

On August 5, 2013, the "Knesset" issued the Law for Changing National Priorities (Legislative Amendments for Achieving Budget Targets for 2013 and 2014), 2013 ("the Budget Law"), which consists, among others, of fiscal changes whose main aim is to enhance the collection of taxes in those years.

These changes include, among others, increasing the corporate tax rate from 25% to 26.5%, cancelling the reduction in the tax rates applicable to privileged enterprises (9% in development area A and 16% elsewhere) and, in certain cases, increasing the rate of dividend withholding tax within the scope of the Law for the Encouragement of Capital Investments to 20% effective from January 1, 2014. There are also other changes such as taxation of revaluation gains effective from August 1, 2013. The provisions regarding revaluation gains will become effective only after the publication of regulations defining what should be considered as "retained earnings not subject to corporate tax" and regulations that set forth provisions for avoiding double taxation of overseas assets. As of the date of approval of these financial statements, these regulations have not been issued.

The deferred tax balances included in the financial statements as of December 31, 2013 are calculated according to the new tax rates that were substantially enacted as of the reporting date and, therefore, comply with the above changes, as applicable to the Company.

The effect of the abovementioned change on the financial statements is immaterial.

c. Tax assessments:

The Company has not received final tax assessments since its incorporation, however, the assessments of the Company are deemed final through 2009.

d. Deferred taxes:

The deferred taxes are reflected in the statement of financial position as follows:

	December 31, 2013	December 31, 2012
Non-current assets	1,593	498

Deferred tax assets are computed at a tax rate of approximately 26.5% and 25% for 2013 and 2012, respectively.

U.S. dollars in thousands

NOTE 16:- TAXES ON INCOME (Cont.)

The Company recorded deferred tax assets, principally for tax loss carryforwards and also for other temporary differences, as of December 31, 2013 and 2012 in the amount of $ 1,593and $ 498, respectively (see e below). The deferred tax assets were recorded based on the Company’s management best estimation of realization of these losses and temporary differences in the foreseeable future.

e. Changes in deferred taxes:

	Year ended December 31,	
	2013	**2012**
Balance at the beginning of the year	498	483
Change during the year	1,095	15
Balance at the end of the year	1,593	498

f. Income tax benefit included in statements of income:

	December 31,	
	2013	**2012**
Current taxes	-	-
Deferred taxes	(1,095)	-
	(1,095)	-

g. Theoretical tax:

The reconciliation between the tax expense, assuming that all the income and expenses, gains and losses in the statement of income were taxed at the statutory tax rate and the taxes on income recorded in profit or loss is as follows:

	Year ended December 31,	
	2013	**2012**
Income before taxes on income	1,832	1,079
Taxes computed at statutory tax rate of 25% (2012- 25%)	458	270
Increase (decrease) in tax due to:		
Non-deductible expenses	1	20
Cost of share-based payments	12	28
Utilization of previously unrecognized tax losses and other items *)	(471)	(318)
Deferred tax assets recorded for carry forwards losses from previous years	(1,095)	-
Income tax benefit	(1,095)	-

U.S. dollars in thousands

NOTE 16:- TAXES ON INCOME (Cont.)

*) Including differences in the basis of measurement (U.S.$ - NIS) - amount represents the difference resulting from the basis of measurement for income tax purposes in Israel (calculated based on the New Israeli Shekel) and the measurement currency of the Company (the U.S. dollars).

h. Carryforward losses for tax purposes:

The Company's carryforward losses for tax purposes as of December 31, 2013 and 2012 amount to approximately $ 16,154 and $ 16,636, respectively. With respect to tax losses carryforward of approximately $ 10,143 and $ 14,644, no deferred tax asset was recognized as of December 31, 2013 and 2012, respectively.

NOTE 17:- COMMITMENTS AND CONTINGENT LIABILITIES

During the reporting period one of the Company's customers filed a lawsuit against the Company on the grounds of a commercial dispute. The customer claims damages and compensation in the amount of NIS 5 million (approx. $ 1.38 million).

Based on the estimation of the Company and its legal advisors, the Company is not expected to pay any material compensation and accordingly the Company did not record any provision for this claim in its financial statements.

NOTE 18:- EQUITY

a. The share capital is composed as follows:

	December 31, 2013		December 31, 2012	
	Authorized	Issued and outstanding	Authorized	Issued and outstanding
	Number of shares			
Ordinary shares of NIS 5 par value each	50,000,000	13,712,848	50,000,000	13,712,848

The authorized share capital of the Company is NIS 250,000,000 comprised of 50,000,000 authorized Ordinary shares, par value NIS 5 each.

b. Stock Option Plan:

1. In June 8, 2005, the Company's Board of Directors adopted a share option plan according to which up to 290,735 options exercisable into Ordinary shares of the Company may be granted to officers, directors, employees and consultants of the Company.

U.S. dollars in thousands

NOTE 18:- EQUITY (Cont.)

2. In May 9, 2006, the BOD resolved to increase the number of shares available for option grants under the June 2005 share option plan up to 500,000 options.

3. In June 14, 2011 additional allocation of 330,000 options to the Company's CEO, directors and top management of Risco Ltd., the controlling shareholders, was approved by the audit committee and the board of directors. The final approval by the Company's share-holders was received on October 10, 2011.

   Measurement of the fair value of equity-settled share options:

   The Company uses the Binomial model when estimating the grant date fair value of equity-settled share options. The measurement was made at the grant date of equity-settled share options since the options were granted to employees.

   The following table lists the inputs to the binomial model used for the fair value measurement of equity-settled share options for the above plan:

Dividend yield	0%
Expected volatility of the share prices	77.3%
Risk-free interest rate	1.89%
Expected life of share options	10 years
Share price	€ 1.010

   Based on the above inputs, the fair value of the options was determined at $ 212 (€ 164) at the grant date.

   The options granted will expire 10 years after the date of grant and vest over a period of 3 years. The exercise price of the options granted is € 1.5.

   The expected life of the share options is based on historical data and is not necessarily indicative of the exercise patterns of share options that may occur in the future.

   The expected volatility of the share prices reflects the assumption that the historical volatility of the share prices is reasonably indicative of expected future trends.

4. Movement during the year:

   The following table illustrates the number and weighted average exercise prices (WAEP) of, and movements in, share options during the years:

U.S. dollars in thousands

NOTE 18:- EQUITY (Cont.)

	Year ended December 31,			
	2013		2012	
	Number of options	WAEP (U.S.$)	Number of options	WAEP (U.S.$)
Share options outstanding at beginning of year	491,181	3.38	541,181	3.25
Share options forfeited during the year	-	-	(50,000)	1.94
Share options outstanding at end of year	491,181	3.38	491,181	3.38
Share options exercisable at end of year	397,848	3.72	294,768	4.18

5. During 2012, the employment of certain officers and employees of the Company, who were previously granted options, was terminated. Consequently 50,000 of the options were forfeited, respectively.

   Total expenses of share-based payments amounted to $ 48 and $ 110 for 2013 and 2012, respectively.

NOTE 19:- FINANCIAL INSTRUMENTS

a. The financial assets and financial liabilities in the statement of financial position are classified by groups of financial instruments pursuant to IAS 39:

	December 31,	
	2013	2012
Financial assets:		
Financial assets at fair value through profit or loss:		
Derivatives	51	27
Loans and receivables	927	658
Financial liabilities:		
Financial liabilities measured at amortized cost	2,068	2,641

NOTE 19:- FINANCIAL INSTRUMENTS (Cont.)

b. Financial risks factors:

The Company's activities expose it to various financial risks such as market risk (foreign exchange risk and interest rate risk), credit risk and liquidity risk. The Company comprehensive risk management plan focuses on activities that reduce to a minimum any possible adverse effects on the Company's financial performance.

The Company's management oversees the risks in accordance with the policies approved by the Board.

1. Market risks:

a) Foreign exchange risk:

The Company operates in a large number of countries and is exposed to foreign exchange risk resulting from the exposure to different currencies. Foreign exchange risk arises on forward commercial transactions, recognized assets and liabilities that are denominated in a foreign currency other than the functional currency. Accounting department is responsible for managing the net position of each foreign currency by the use of forward exchange contracts and other hedging tools.

Management's policy is to hedge between 40% and 70% of forecasted transactions in every principal currency over the next 12 months.

The Company has forward foreign currency contracts and cylinder transactions to manage some of its transactions exposure to fluctuations in exchange rates. These forward foreign currency contracts and cylinder transactions are not designated as cash flow, fair value or net investment hedges and are entered into the periods consistent with the periods of currency transaction exposure. Such derivatives do not qualify for hedge accounting.

As of December 31, 2013 and 2012, the Company's monetary assets in NIS exceeded monetary liabilities by $ 820 and $ (372), respectively.

As of December 31, 2013 and 2012, the Company's monetary assets in Euro exceeded monetary liabilities by $ 485 and $ 136, respectively.

As of December 31, 2013 and 2012, the Company's monetary assets in GBP exceeded monetary liabilities by $ 393 and $ 235, respectively.

b) Interest rate risk:

The Company is exposed to the risk of changes in the market interest rates on long-term loans with floating interest rates. As of December 31, 2013 the exposure is immaterial.

NOTE 19:- FINANCIAL INSTRUMENTS (Cont.)

2. Credit risk:

The Company monitors and reduces its credit risk by using a policy to ensure collection through sales of its products to wholesalers with an appropriate credit history and by insuring the customers who received a credit line.

Credit risk may arise from the exposure of holding several financial instruments with a single entity or from entering into transactions with several groups of debtors with similar economic characteristics whose ability to discharge their obligations will be similarly affected by changes in economic or other conditions. Factors that have the potential of creating concentrations of risks consist of the nature of the debtors' activities, such as their business sector, the geographical area of their operations and the financial strength of groups of borrowers.

The Company regularly monitors the credit extended to its customers. The Company provides an allowance for doubtful accounts based on the factors that affect the credit risk of certain customers, past experience and other information.

3. Liquidity risk:

The Company monitors its risk to a shortage of funds using a monthly and daily budget tool.

The Company's objective is to maintain a balance between continuity of funding and flexibility through the use of bank overdrafts and bank loans.

The maturities of the financial liabilities of the Company are for one year, except for the bank loans. The long-term loans are repayable in future years based on contractual undiscounted payments, as follows:

	December 31,	
	2013	**2012**
First year	2,068	2,462
Second year	-	179
	2,068	2,641

c. Fair value:

The carrying amount of cash and cash equivalents, trade receivables, other accounts receivable, credit from banks, trade payables and other accounts payable approximate their fair value.

U.S. dollars in thousands

NOTE 19:- FINANCIAL INSTRUMENTS (Cont.)

d. Classification of financial instruments by fair value hierarchy:

The financial instruments presented in the balance sheet at fair value are with similar characteristics using the following fair value hierarchy (level 3 - valuation techniques which use inputs that are not based on observable market data).

Financial assets measured at fair value- Derivatives – level 3

	December 31,	
	2012	**2011**
Financial assets at fair value through profit or loss:	51	27

e. Sensitivity analysis relating to changes in market factors:

	December 31,	
	2013	**2012**
Sensitivity analysis to changes in the NIS exchange rate:		
Gain (loss) from the change:		
Increase of 5% in the NIS rate	(79)	(82)
Decrease of 5% in the NIS rate	79	82
Sensitivity analysis to changes in the Euro exchange rate:		
Gain (loss) from the change:		
Increase of 5% in the Euro rate	24	7
Decrease of 5% in the Euro rate	(24)	(7)
Sensitivity analysis to changes in the GBP exchange rate:		
Gain (loss) from the change:		
Increase of 5% in the GBP rate	20	12
Decrease of 5% in the GBP rate	(20)	(12)

NOTES TO FINANCIAL STATEMENTS

U.S. dollars in thousands

NOTE 20:- REVENUES

a. Foreign:

	Year ended December 31, 2013	Year ended December 31, 2012
Europe	14,814	12,115
Americas	547	550
Other countries	1,164	1,634
	16,525	14,299
Domestic - Israel	9	32
	16,534	14,331

b. Additional information about revenues:

Revenues from major customers which each account for 10% or more of total revenues as reported in the financial statements:

	Year ended December 31, 2013	Year ended December 31, 2012
Customer A	3,840	2,652
Customer B (Fellow subsidiary)	2,329	1,957
Customer C	2,327	2,106
	8,496	6,715

NOTE 21:- COST OF REVENUES

	Year ended December 31, 2013	Year ended December 31, 2012
Purchases and changes in raw materials	8,748	10,604
Labor	531	432
Manufacturing and other expenses (Including insurance reimbursement for prior year claim)	(33)	499
Depreciation	216	198
	9,462	11,733
Changes in inventories of finished products and work-in-progress	45	(2,726)
	9,507	9,007

U.S. dollars in thousands

NOTE 22:- RESEARCH AND DEVELOPMENT EXPENSES

	Year ended December 31, 2013	Year ended December 31, 2012
Salaries and related expenses	588	555
Consulting fees	607	630
Other	40	62
	1,235	1,247

NOTE 23:- SELLING AND MARKETING EXPENSES

	Year ended December 31, 2013	Year ended December 31, 2012
Salaries and related expenses	987	900
Advertising	180	100
Foreign travel and transportation	222	188
Other	462	368
	1,851	1,556

NOTE 24:- GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended December 31, 2013	Year ended December 31, 2012
Salaries and related expenses	677	644
Management and consulting fees	837	427
Depreciation	75	75
Other	558	532
	2,146	1,678

U.S. dollars in thousands

NOTE 25:- OTHER EXPENSES, NET

	Year ended December 31, 2013	Year ended December 31, 2012
Capital loss (gain) on sale of property, plant and equipment	-	2
Other income (settlement of lease)	-	(404)
	-	(402)

NOTE 26:- FINANCIAL INCOME AND EXPENSES

	Year ended December 31, 2013	Year ended December 31, 2012
a. Financial income:		
Foreign exchange differences	167	-
	167	-
b. Financial expenses:		
Bank borrowings, net	129	128
Other (Including foreign exchange differences in 2012)	1	38
	130	166

NOTES TO FINANCIAL STATEMENTS

U.S. dollars in thousands

NOTE 27:- NET PROFIT PER SHARE

The following reflects the net profit and share data used in the basic and diluted net profit per share computations:

	Year ended December 31, ,	
	2013	2012
Profit attributable to Ordinary shares for computing basic and diluted net loss per share	2,927	1,079
Weighted average number of Ordinary shares for computing basic net profit (loss) per share	13,712,848	13,712,848
Adjusted weighted average number of Ordinary shares for computing diluted profit (loss) per share	13,712,848	13,712,848

In the calculation of the diluted net profit per share for the years ended December 31, 2013 and 2012, all share options were not taken into account because of the anti-dilutive effect.

NOTE 28:- BALANCES AND TRANSACTIONS WITH RELATED PARTIES

a. Balances with related parties:

	December 31,	
	2013	2012
Trade payables - Parent company, fellow subsidiary and related party	(765)	(1,048)
Trade receivable - Fellow subsidiary	364	194
Key management personnel (including directors)	(24)	(26)

b. Transactions with related parties:

	December 31,	
	2013	2012
Manufacturing services agreement (see d 2 below):		
Raw material sales *)	(379)	(115)
Purchases of finished goods	1,675	4,571
Management service agreement (see d 1 below)	800	300
Research and development services (see e below)	541	592
Distribution agreement (see d 3 below)	(2,338)	(1,989)
Finder fees	38	-
Key management personnel (including directors)	245	223

*) Based on Company's cost used for manufacturing.

NOTE 28:- BALANCES AND TRANSACTIONS WITH RELATED PARTIES (Cont.)

c. On July 10, 2012 the Company's audit committee and board of directors approved a settlement agreement with the Company's previous management. According to the settlement agreement, the Company paid its previous management an amount of $ 86 to remove any future claims regarding to management's services provided according to past service agreement.

d. After approval by the Company's audit committee, the shareholders, in a special general meeting on August 12, 2010, approved the agreement that the Company had entered into with Risco, which includes the following:

1. Management services agreement - Risco is willing to exert its efforts and utilize its professional connections in order to assist the Company in the following fields: (i) sales administration services; (ii) IT and computerized systems; (iii) finance management and accounting; (iv) human resource; (v) directors and consulting services; (vi) legal and company secretarial services.

   The Company shall pay Risco for all services rendered by it under this agreement, payable not less often than monthly and in accordance with the Company's normal and reasonable payment payroll practices regarding service providers, an annual gross amount of $ 300. The annual amount shall be adjusted on a yearly basis in accordance with the change in the Company's revenues from sales compared to the revenue from sales of the preceding year, but in any event shall not be less than the base amount.

2. Manufacturing services agreement - the Company wishes to retain Risco services for the purpose of manufacturing certain products of the Company, on a non-exclusive basis. Prices shall be provided by the service provider, and agreed on by the parties.

3. Distribution agreement - Risco has the facilities to import, promote, sell, market and distributes the products in the territory (as defined in the agreement) and is willing to act as the supplier's non-exclusive distributor of the products in the territory. The distributor and supplier intend that the transfer prices for the products shall be, in the aggregate for all products for each calendar year, at arm's length prices.

e. After approved by the Company's audit committee and the Company's shareholders, on June 16, 2011, the Company had entered into an R&D service agreement with a service provider controlled by the controlling shareholder of the Company's largest and controlling shareholder.
On April 8, 2014 the Company’s audit committee and the Company's board of directors approved a three year extension of the R&D service agreement.
The extension of the R&D service agreement is subject to the approval of the Company’s shareholders.

U.S. dollars in thousands

NOTE 28:- BALANCES AND TRANSACTIONS WITH RELATED PARTIES (Cont.)

f. After approved by the Company's audit committee, the shareholders, in a special general meeting on October 10, 2012 approved an amendment to the Distribution agreement with Risco (see d 3 above). According to the amendment the Company will have the option to distribute Risco products.

g. On August 29, 2013, the Company's shareholders approved the agreement that the Company had entered into with Risco, which includes the following:

1. A three year extension of the Manufacturing services agreement with the parent company (Risco).

2. An amendment to the Management services agreement with the parent company (Risco) (see d 1 above). The revised agreement includes; (i) additional services which will be rendered by Risco to the Company and (ii) revises the annual amount payable to Risco so that the base amount will be an amount of $800 instead of $300, and (iii) the agreement has been extended for an additional three years period.

The revised Management Services Agreement shall be in effect for a term of 3 years as of January 1, 2013.

h. On April 14, 2013, the board of directors and the compensation committee recommended the approval of the Company's Compensation Policy in respect of the Company's CEO. On August 29, 2013, the Company's shareholders approved the Company's Compensation Policy.

The compensation policy includes base salary increase and annual sales commission in accordance to accomplishment of the sales and gross profit targets.
The Compensation Policy is a multi-year policy which shall be in effect for a period of three years from the date of its approval.

NOTE 29:- GEOGRAPHICAL INFORMATION

Revenues reported in the financial statements derive from the Company's country of domicile (Israel) and foreign countries based on the location of the customers, are as follows:

	Year ended December 31,	
	2013	2012
Israel	9	32
Europe	14,814	12,115
Other foreign countries	1,711	2,184
	16,534	14,331

U.S. dollars in thousands

NOTE 29:- GEOGRAPHICAL INFORMATION (Cont.)

The carrying amounts of non-current assets (property, plant and equipment and intangible assets) in the Company's country of domicile (Israel) and in foreign countries based on the location of the assets, are as follows:

	December 31,	
	2013	2012
Israel	446	579
Foreign countries	330	333
	776	912

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