TEFRON LTD

CONSOLIDATED FINANCIAL STATEMENTS
AS AT DECEMBER 31, 2017

IN DOLLARS THOUSANDS

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Consolidated Financial Statements as at December 31, 2017

In Dollars Thousands

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Deloitte.

Auditor's Report

To the Shareholders of Tefron Ltd.

We have audited the accompanying consolidated balance sheets of Tefron Ltd. (hereinafter -"the Company") as at December 31, 2017 and 2016, and the consolidated statements of income, comprehensive loss, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2017. These financial statements are the responsibility of the Company's Board of Directors and management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, based on our audit, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company and its subsidiaries as at December 31, 2017 and 2016, and the results of their operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2017, in conformity with the International Financial Reporting Standards ("IFRS") and with the provisions of the Israeli Securities Regulations (Annual Financial Statements), 2010.

Respectfully,

Brightman Almagor Zohar & Co.
Certified Public Accountants
Member of Deloitte Touche Tohmatsu Limited

Haifa, March 29, 2018

Tefron Ltd.

Consolidated Balance Sheets

	Note	As at December 31 2017	2016
		Dollars thousands	
Current assets			
Cash		1,220	1,354
Trade receivables, net	5	17,714	16,681
Other receivables	6	3,244	4,129
Inventory	7	25,684	24,574
		47,862	46,738
Non-current assets			
Property, plant and equipment, net	8	21,554	24,348
Goodwill and intangible assets, net	9a	75	213
Computer software, net	9b	1,612	1,367
Long-term receivables		118	-
Deferred taxes, net	17	2,890	2,890
		26,249	26,818
		74,111	75,556

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

Tefron Ltd.

Consolidated Balance Sheets

	Note	As at December 31 2017	As at December 31 2016
		Dollars thousands	
Current liabilities			
Bank credit	10	14,185	15,156
Trade payables	11	21,854	17,898
Other payables	12	2,136	2,546
		38,175	35,600
Non-current liabilities			
Long-term loans from banks and vendors	13	9,202	10,826
Subordinated loan from the shareholders		1,852	-
Liabilities for bank options	15	20	95
Liabilities for benefits to employees, net	16	1,000	797
Long-term payables	18	-	1,043
		12,074	12,761
Equity attributed to the Company's shareholders	20		
Share capital		33,617	33,617
Additional paid-in capital		99,686	99,686
Capital reserve for remeasurement of defined benefit plans		(1,541)	(1,259)
Accumulated deficit		(100,830)	(97,631)
Treasury shares		(7,408)	(7,408)
Other capital reserves		338	190
Total equity		23,862	27,195
		74,111	75,556

March 29, 2018			
Date of approval of the financial statements	**Arnon Tiberg** **Chairman of the Board**	**Ben Lieberman** **CEO**	**Eliezer Parnafes** **CFO**

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

Tefron Ltd.

Consolidated Statements of Income

	Note	For the year ended December 31 2017	2016	2015
		Dollars thousands (excluding data on loss per share)		
Sales		121,499	116,402	93,086
Cost of sales	22a	99,103	92,531	74,582
Gross profit		,22396	23,871	18,504
Development expenses, net	22b	4,468	3,991	3,694
Selling and marketing expenses	22c	15,479	13,401	12,760
General and administrative expenses	22d	2,985	3,055	2,914
Other expenses (income)	22e	(235)	1,099	817
Operating profit (loss)		(301)	2,325	(1,681)
Financial income	22f	75	9	471
Financing expenses	22f	(2,892)	(2,673)	(2,728)
Financing expenses, net		(2,817)	(2,664)	(2,257)
Loss before taxes on income		(3,118)	(339)	(3,938)
Taxes on income	17	(81)	(782)	-
Loss for the year		(3,199)	(1,121)	(3,938)
Loss per share attributable to equity shareholders of the Company	23			
Basic and diluted loss per share		(0.27)	(0.09)	(0.41)

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

Tefron Ltd.

Consolidated Statements of Comprehensive Loss

	For the year ended December 31		
	2017	2016	2015
	Dollars thousands		
Loss	(3,199)	(1,121)	(3,938)
Other comprehensive loss (after the effect of the tax):			
Amounts that will not be reclassified subsequently to the statements of income:			
Loss for re-measurement of defined benefit plan	(282)	(27)	(123)
Subtotal of items that will not be reclassified subsequently to the statements of income	(282)	(27)	(123)
Amounts that will be reclassified or are reclassified to the statements of income provided that specific terms are met:			
Loss realized for cash flow hedging transactions	-	-	30
Transfer to the statement of income on disposal of investments in securities available for sale	-	-	97
Subtotal of items that will be reclassified or are reclassified to the statements of income	-	-	127
Total other comprehensive income (loss)	(282)	(27)	4
Total comprehensive loss attributed to the Company's shareholders	(3,481)	(1,148)	(3,934)

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

Tefron Ltd.

Consolidated Statements of Changes in Shareholders' Equity

	Relating to the Company's shareholders						
	Share capital	Additional paid-in capital	Reserve for actuarial losses	Accumulated deficit	Treasury shares	Other capital reserves	Total equity
	Dollars thousands						
Balance as at January 1, 2017	33,617	99,686	(1,259)	(97,631)	(7,408)	190	27,195
Loss	-	-	-	(3,199)	-	-	(3,199)
Total other comprehensive loss	-	-	(282)	-	-	-	(282)
Subordinated loan from the shareholders	-	-	-	-	-	148	148
Balance as at December 31 , 2017	33,617	99,686	(1,541)	(100,830)	(7,408)	338	23,862

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

Tefron Ltd.

Consolidated Statements of Changes in Shareholders' Equity

	Relating to the Company's shareholders						
	Share capital	Additional paid-in capital	Reserve for actuarial losses	Accumulated deficit	Treasury shares	Other capital reserves	Total equity
	Dollars thousands						
Balance as at January 1, 2016	33,617	99,627	(1,232)	(96,510)	(7,408)	237	28,331
Loss	-	-	-	(1,121)	-	-	(1,121)
Total other comprehensive loss	-	-	(27)	-	-	-	(27)
Share based payment to employees and directors	-	12	-	-	-	-	12
Expiry of rights to shares of the consultant	-	47	-	-	-	(47)	-
Balance as at December 31 , 2016	33,617	99,686	(1,259)	(97,631)	(7,408)	190	27,195

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

Tefron Ltd.

Consolidated Statements of Changes in Shareholders' Equity

	Relating to the Company's shareholders								
	Share capital	Additional paid-in capital	Reserve for actuarial losses	Accumulated deficit	Treasury shares	Capital reserve for financial assets available for sale	Capital reserve for hedging transactions	Other capital reserves	Total equity
	Unaudited								
	Dollars thousands								
Balance as at January 1, 2015	20,281	107,467	(1,109)	(92,572)	(7,408)	(97)	(30)	272	26,804
Loss	-	-	-	(3,938)	-	-	-	-	(3,938)
Total other comprehensive loss	-	-	(123)	-	-	97	30	-	4
Share-based payment to employees and directors	-	36	-	-	-	-	-	-	36
Expiry of rights to shares of the consultant	-	35	-	-	-	-	-	(35)	-
Private placement (less issue expenses of 100 thousand dollars)	13,336	(7,911)	-	-	-	-	-	-	5,425
Balance as at December 31, 2015	33,617	99,627	(1,232)	(96,510)	(7,408)	-	-	237	28,331

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

Tefron Ltd.

Consolidated Statements of Cash Flows

	For the year ended December 31		
	2017	2016	2015
	Dollars thousands		
Cash flows from operating activities			
Loss	(3,199)	(1,121)	(3,938)
Adjustments required to present cash flows from operating activities:			
Adjustments to the statement of income items:			
Depreciation and amortization:			
Depreciation and amortization of fixed and intangible assets	4,940	5,257	4,898
Gain due to the cancellation of a provision for impairment	(351)	-	-
Cost of share based payments	-	12	36
Loss from impairment of slow inventory	627	436	433
Loss from disposal of securities available for sale	-	-	169
	5,216	5,705	5,536
Change in deferred taxes, net	-	340	-
Change in liabilities for benefits to employees, net	(79)	8	(144)
Change in fair value of liabilities for bank options	(75)	(9)	84
Taxes on income	415	303	291
Financing expenses, net	1,998	1,926	1,565
	2,259	2,568	1,796
Changes in assets and liabilities items:			
Decrease (increase) in trade receivables	(1,033)	163	1,178
Decrease (increase) in other receivables	767	(1,091)	(502)
Increase in inventory	(1,737)	(6,186)	(3,908)
Increase (decrease) in trade payables	4,124	3,724	(867)
Decrease (increase) in other payables	(410)	234	(78)
	1,711	(3,156)	(4,177)
Cash paid and received during the year for:			
Interest paid	(1,972)	1,897	(1,524)
Interest received	-	6	2
Taxes paid	(415)	(303)	(291)
	(2,387)	(2,194)	(1,813)
Net cash provided from (used for) operating activities	3,600	1,802	(2,596)

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

Tefron Ltd.

Consolidated Statements of Cash Flows

	For the year ended December 31		
	2017	2016	2015
	Dollars thousands		
Cash flows from investing activities			
Purchase of fixed assets	(1,491)	(1,815)	(1,235)
Purchase of software	(411)	(286)	(887)
Proceeds from disposal of securities available for sale	-	-	310
Net cash used for investing activities	(1,902)	(2,101)	(1,812)
Cash flows from financing activities			
Short-term bank credit, net	(971)	3,756	2,265
Repayment of long-term loans	(1,650)	(1,650)	(1,923)
Repayment of long-term credit for fixed assets	(1,211)	(1,217)	(626)
Subordinate loan from the shareholders	2,000	-	-
Debt settlement expenses	-	-	(193)
Proceeds from a private placement (less issue expenses)	-	-	5,425
Net cash provided by (used for) financing activities	(1,832)	889	4,948
Increase (decrease) in cash and cash equivalents	(134)	590	540
Balance of cash and cash equivalents at beginning of year	1,354	764	224
Balance of cash and cash equivalents at end of year	1,220	1,354	764

	For the year ended December 31		
	2017	2016	2015
	Dollars thousands		
(A) Non-cash significant transactions			
Acquisition of fixed assets on credit (see Note 8e as follows)	-	-	2,750
Acquisition of assets through an exchange	-	-	128
Disposal of assets through an exchange	-	-	-

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

Note 1 - General

a. Tefron Ltd. (hereinafter: "the Company") is a company registered in Israel. The Company's production operations are carried out through subcontractors as well as by a self-production process in plants located in the Far East, Israel and Jordan. The Company and its subsidiaries focus on the development, production, marketing and sale of intimate apparel and activewear which are sold throughout the world to companies with leading brands. The Company operates in two operating business segments – brands and retail. For details regarding the business segments and operating markets, see Note 24 below.

The Company’s shares are traded on the Tel Aviv Stock Exchange. For additional details, also see Note 20.

The Company's head offices are located in the industrial area of "Misgav”, Israel.

b. Definitions

In these financial statements:

The Company	-	Tefron Ltd.
The Group	-	Tefron Ltd. and its subsidiaries as detailed in the attached list.
Subsidiaries	-	Companies in which the Company has control of (as defined in IFRS 10) and whose statements are consolidated with those of the Company.
Related parties	-	As defined in IAS 24.
Interested parties and controlling shareholder	-	As defined in the Securities Regulations (Annual Financial Statements), 2010.

Note 2 - Significant accounting principles

The accounting principles as detailed as follows were used consistently throughout the financial statements, throughout all the periods presented, unless it is noted otherwise.

a. Basis of presentation of the financial statements

The financial statements are prepared in accordance with the International Financial Reporting Standards (hereinafter: "IFRS").
Furthermore, the financial statements are prepared in accordance with the Israeli Securities Regulations (Annual Financial Statements), 2010.

The Company's financial statements are prepared on the basis of cost, excluding derivatives and financial assets available for sale; financial assets and liabilities (including derivative instruments) which are presented at fair value through the statement of income which are measured according to their fair value and excluding liabilities for employee benefits.
The Company has chosen to present the items in the statements of income according to the nature-of-expense method.

b. Consolidated financial statements

The consolidated financial statements include the statements of companies controlled by

Note 2 - Significant accounting principles (cont.)

b. Consolidated financial statements (cont.)

the Company (wholly-owned subsidiaries). Control exists when the Company has influence on the investee entity, exposure or rights to variable returns as a result of its involvement in the investee entity, as well as the ability to use its power to influence the sum of returns that shall derive from the investee entity. While assessing control, one takes into account the influence of the potential voting rights, only if they are substantive. The consolidation of the financial statements commences as of the date on which control is obtained and ends when such control ceases.

The financial statements of the Company and its subsidiaries are prepared for identical dates and periods. The Company's accounting policy in the financial statements of its subsidiaries was implemented uniformly and consistently with the one implemented in the Company's own financial statements. Significant intra-group balances and transactions, and any profits and losses resulting from intra-group transactions were eliminated in full in the consolidated financial statements.

c. Functional, presentation and foreign currency

1. Functional and presentation currency

The presentation currency of the financial statements is the US dollar.

The functional currency which is the currency that best reflects the economic environment in which the Company operates and conducts its transactions, is determined separately for each entity in the Group, and according to this functional currency its financial position and operating results are measured.
The Group determines the functional currency of the Company for each entity of the Group.
The functional currency of the Company is the US dollar.

2. Transactions, assets and liabilities in foreign currency

Transactions denominated in foreign currency are recorded initially at the exchange rate on the date of the transaction. After the initial recognition, monetary assets and liabilities that are denominated in foreign currency are translated on each balance sheet date into the functional currency, at the exchange rate on that date. Exchange rate differences, other than those that are discounted to qualifying assets or are recognized in equity in hedging transactions, are recognized in the statement of income. Non-monetary assets and liabilities denominated in foreign currency and presented by cost are retranslated according to the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currency and presented at fair value are translated into the functional currency, in accordance with the rates of exchange on the date on which the fair value is determined.

d. Exclusion of separate financial information in the framework of the periodic reports

In the framework of the periodic reports for 2017 the Company did not include separate financial information in accordance with Regulation 9c and the Tenth Addendum to the Securities Regulations (Periodic and Immediate Reports -1970) since the Company believes the information contained in it is negligible from a qualitative standpoint, in spite of its quantitative scope, the reason for which is mainly due to the fact that as stated in Note 13b, the Group's credit agreements with the lending banks refer to the Tefron Group as a whole with cross-guarantees between the entities of the Group and

Note 2 – Significant accounting principles (cont.)

d. Exclusion of separate financial information in the framework of the periodic reports (cont.)

providing information regarding separate financial statements will not carry with it any additional material information to the reasonable investor (shareholder) or to the creditors regarding the liquidity risk of the parent company, that is not already included in the framework of the consolidated financial statements of the Company.

e. Allowance for doubtful accounts

The allowance for doubtful accounts is determined specifically in respect of trade receivables whose collection, in the opinion of the Company's management, is doubtful. Impaired trade receivables will be withdrawn once they are assessed as uncollectible. The Company does not carry out any further review at the level of the customer groups for those for which no allowance for impairment has been made separately, as aforementioned, since it believes that it has no material impact on the financial statements.

f. Inventory

Inventory is measured at the lower of cost or net realizable value. The cost of inventory includes the expenses for purchasing the inventory as well as other costs incurred in bringing it to its current 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 costs necessary to carry out the sale. The Company periodically evaluates the condition and age of inventory and records provisions for slow-moving inventory accordingly.

The cost of inventories is determined as follows:

Raw materials	-	Based on cost by the weighted average method.
Work in progress and finished goods	-	Based on average cost including material, labor and other direct and indirect manufacturing costs.

g. Revenue recognition

Revenues are recognized in the statement of income when they can be measured in a reliable fashion, it is expected 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 in a reliable fashion. The revenues are measured at the fair value of the consideration received in the transaction less any trade discounts, volume rebates and returns.
The specific criteria regarding revenue recognition which are required to be fulfilled prior to the revenue recognition are as follows:
Regarding the publication of final standard IFRS 15 "Revenues from contracts with customers", see Note 4a.

Revenues from the sale of goods

Revenues from the sale of goods are recognized once the significant risks and rewards derived from the ownership of the goods have been transferred to the buyer and the seller no longer retains any continued managerial involvement. Usually the date of the delivery is the date on which the ownership was transferred.

Note 2 – Significant accounting principles (cont.)

g. Revenue recognition (cont.)

Discounts to customers

Discounts given to customers at the end of the year, for which the customer is not required to meet certain objectives, are included in the financial statements upon reaching the proportional sales which entitle the customer to these discounts and are deducted from the sales item.

h. Government grants

Government grants relating to assets such as fixed assets are presented as a deduction of the assets for which the grants were received.

i. Taxes on income

Taxes on income in the statements of income include deferred taxes. The tax results in respect of deferred taxes are recorded to the statement of income except to the extent that the tax arises from items which are recognized directly to shareholders' equity. In such cases, the tax effect is also recorded to the relevant item in shareholders' equity.

Deferred taxes

Deferred taxes are computed for temporary differences between the carrying amounts in the financial statements and the amounts attributed for tax purposes.
Deferred tax balances are measured at the tax rate that is expected to apply once the asset is realized or the liability is settled, based on tax laws that have been enacted or substantively enacted until the balance sheet date.
Deferred tax assets are reviewed on each balance sheet date and reduced to the extent that it is not probable that they will be utilized, temporary differences for which deferred tax assets have not been recognized, are reassessed on each balance sheet date and if their recoverability has become probable, an appropriate deferred tax asset is recognized.

When computing deferred taxes, taxes that would have applied in the event of the sale of investments in investee companies have not been taken into account, as long as it is probable that the sale of the investments in investee companies is not expected in the foreseeable future. Moreover, deferred taxes that would have applied in the event of distribution of earnings by investee companies as dividends have not been taken into account in computing deferred taxes, since the distribution of dividends does not involve an additional tax liability or since it is the Company's policy not to initiate distribution of dividends by a subsidiary since it involves an additional tax liability.
Deferred tax assets and deferred tax liabilities are presented in the balance sheet as non-current assets and non-current liabilities, respectively. Deferred taxes are offset if there is a legally enforceable right to set off a current tax asset against a current tax liability and the deferred taxes relate to the same taxable entity and the same tax authority.

j. Discontinued operation

Discontinued operation is a component of the Company which constitutes operation that was realized or classified as held for sale, the results of the operation relating to the discontinued operation are presented separately in the statement of income, less the tax effect.

Note 2 – Significant accounting principles (cont.)

k. Leasing

The tests for classifying leases as finance or operating leases depend on the substance of the agreements and they are reviewed at the inception of the lease in accordance with the principles below as set out in IAS 17:

The Group as a lessee

Operating lease

Assets, for which all risks and rewards inherent in the ownership of the leased asset are not actually transferred, are classified as operating lease. The lease fees are recognized as an expense in the statement of income on a straight-line basis continuously over the lease period.

The Group as a lessor

Operating lease

Assets, for which all risks and rewards related to the ownership of the leased asset are not actually transferred, are classified as operating lease. The lease fees are recognized as an expense in the statement of income on a straight-line basis continuously over the lease period.

l. Fixed assets

Items of fixed assets are presented at cost plus direct acquisition costs less any accumulated depreciation, less accumulated impairment losses and less related investment grants and excluding day-to-day maintenance expenses. Cost includes spare parts and auxiliary equipment that can be used only in connection with machinery and equipment:

	%
Land and buildings	2
Machinery and equipment (mainly 6.67%)	5-15
Office furniture and equipment (mainly 10%)	-610
Leasehold improvements	see below

Leasehold improvements are depreciated using the straight line method over the lease period or over the expected useful life of the improvement, whichever is shorter.

The useful life, depreciation method and residual value of an asset are reviewed at least at the end of each year and the changes are accounted for as a change in accounting estimate in way of prospective application. As for testing the impairment of fixed assets, see Clause o, as follows.

The depreciation of assets is discontinued on the earlier of the date when the asset is classified as held for sale and the date on which the asset is withdrawn.

m. Investment Property

Investment property comprises real estate (land or building) held by the Group for the purpose of earning rentals or for capital appreciation or both, rather than for use in the production or supply of goods or services, or for administrative purposes and not for use in the production or supply of goods or services or for administrative purposes, or sale in the ordinary course of business.

The investment property of the Group includes buildings and land that are owned or leased under a finance lease. Investment property is initially recognized at cost which includes transaction costs, as well as costs which can be directly attributed to bringing

Note 2 – Significant accounting principles (cont.)

m. Investment Property (cont.)

the asset to the condition necessary for it to be used in the manner intended by the management. In the periods subsequent to the initial recognition, the investment property is presented in the consolidated balance sheets at cost less accumulated depreciation and less accumulated impairment losses.

Depreciation of investment property is carried out by using the straight-line method over its estimated useful life from the date on which the asset is ready for its intended use. The depreciation expenses are recognized in the statements of income.

n. Computer software

The Group's assets include computer systems that are comprised of software and licenses. Software forming an integral part of the hardware to the extent that the hardware cannot function without the programs installed on it, is classified as fixed assets. In contrast, stand-alone software licenses that add additional functionality to the hardware are classified as computer software.

Cost of software is measured on initial recognition at cost with the addition of costs directly attributable to the acquisition and capitalization of the expenses related to their cost.

The useful lifespan of the software is as follows:

	%
Computer software	25-33
ERP system	10

o. Intangible assets

Separately acquired intangible assets are measured on initial recognition at cost with the addition of costs directly attributable to the acquisition. Intangible assets acquired in a business combination are included at fair value at the acquisition date. 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 period of amortization and method of amortization of an intangible asset is examined at least at the end of each year.

The useful lifespan of the intangible assets is as follows:

	Years
Customer lists	8

Goodwill is not amortized methodically and is subject to consideration of its loss of impairment on a yearly basis, as well as any time there is an indication that there might be a loss from impairment (see also Note 9a, as follows).

Profits or losses arising from the derecognition of an intangible asset are measured by the difference between the proceeds from the realization, net and the cost of the asset, and are recorded in the statement of income.

Note 2 – Significant accounting principles (cont.)

p. Impairment of non-financial assets

The Company examines the need to record an impairment of the carrying amount of non-financial assets whenever there are indications resulting from events or changes in circumstances which indicate that the carrying amount in the financial statements is not recoverable. In cases where the carrying amount of non-financial assets in the financial statements exceeds their recoverable amount, the assets are reduced to their recoverable amount. The recoverable amount is the higher of the fair value less costs for sale and the value of its use. In evaluating the value of use, the expected cash flows are discounted according to the discounting rate before tax, which reflects the specific risks of every asset. For an asset that does not create independent cash flows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recorded in the statement of income in accordance with the nature of the item whose value declines.

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 date on which the impairment loss was recognized. Reversal of an impairment loss, as aforementioned, is limited to the lower of the amount of impairment recognized in the past (less depreciation or amortization) or the asset’s recoverable amount. A reversal of that impairment loss, as aforementioned, is recognized in the statement of income in the same section in which the impairment was recognized.

The following unique criteria are applied in assessing impairment of the goodwill:

Goodwill

The Company reviews goodwill for impairment once a year on December 31, or more frequently if events or changes in circumstances indicate that impairment can be recognized.
Impairment is recognized for goodwill by reviewing the recoverable amount of the cash-generating unit (or a group of cash-generating units) to which the goodwill has been allocated. When the recoverable amount of the cash-generating unit (or a group of cash-generating units) is lower than the carrying amount in the financial statements of the cash-generating unit (or a group of cash-generating units), to which the goodwill has been allocated, it is recognized as a loss from impairment initially related to goodwill. Losses recognized for goodwill are not reversed in consecutive periods.

q. Financial assets

General:

Financial assets are recognized in the balance sheet when the Group becomes a party to the contractual provisions of the instrument. Where purchase or sale of an investment are under a contract whose terms require transfer of the investment within the timeframe acceptable by the related market, the investment is recognized or derecognized at the time of trade (the date on which the Group has committed to purchase or sell an asset).

Investments in financial assets are initially recognized at fair value plus directly attributable transaction costs, excluding financial assets which are classified at fair value through income statement, which are initially recognized at fair value.

Note 2 – Significant accounting principles (cont.)

q. Financial assets (cont.)

General (cont.):

When the estimated fair value of financial assets that are not traded in an active market includes assumptions that are not supported by observable market prices or rates, the instrument is recognized initially at the transaction price which includes deferred gain or loss resulting from the difference between the estimated fair value and the consideration paid or received. In consecutive periods, the deferred gain or loss will be recognized in income statement only if there have been changes in variables, which market participants take into account when pricing financial assets.

Financial assets are classified into the following categories. The classification into these categories depends on the nature of and purpose of holding the financial asset and it is determined at the time of initial recognition of the financial asset, or at the consecutive reporting periods in cases where these financial assets can be reclassified into another category:

- Loans and receivables; as well as
- Financial assets available for sale

Regarding the publication of the final standard IFRS 9 "Financial Instruments", see Note 4b.

Loans and receivables:
Trade receivables, deposits, loans and other receivables with fixed payments or determinable payments that they are not quoted in an active market are classified as loans and receivables. Loans and receivables are measured at amortized cost using the effective interest method less impairment, if such is detected. Interest income is recognized using the effective interest method, except for short-term receivables when the interest amounts to be recognized are not material.

Impairment of financial assets:

Financial assets, except for those classified as financial assets at fair value through income statement, are reviewed at the end of each reporting period in order to identify indications of impairment. Such impairment occurs when there are objective evidences that, as a result of one or more events that occurred after the initial recognition of the financial asset, the expected future cash flows of the investment were adversely affected by those.

In investments in equity instruments classified as available-for-sale, a significant or prolonged decline in the fair value below their cost is an indication of impairment.

For other financial assets, including trade receivables and finance lease receivables, indications of impairment may include:

- Significant financial difficulties of the issuer or debtor;
- Failure to comply with current payments of principal or interest;
- Probability that the debtor will enter bankruptcy or restructuring of debt.

In respect of certain financial assets, such as trade receivables for whom no indications of impairment have been detected, the Group tests on a group basis, the existence of impairment, based on past experience with groups of debtors that have similar characteristics and changes in the arrears in installments, as well as economic changes related to the sector and the economic environment in which they operate.

Note 2 – Significant accounting principles (cont.)

q. Financial assets (cont.)

Impairment of financial assets (cont.):

For financial assets at amortized cost, impairment is recognized that is equal to the difference between the carrying amount of the financial assets and the current value of estimated future cash flows when they are discounted at the original effective interest rate.

When there is objective evidence of impairment as aforementioned, regarding financial assets available for sale, the cumulative loss recognized in other comprehensive income due to the decrease in the fair value of the financial assets is reclassified to income statement. Impairment losses recognized in income statement, as aforementioned, in respect of an investment in an equity instrument classified as available for sale, are not reversed through income statement. Any increase in the fair value of investments in equity instruments classified as available for sale in the period following the period in which the impairment loss was recognized, is recognized in other comprehensive income.

With the exception of equity instruments classified as available for sale, if in a consecutive period the amount of impairment loss of financial assets is small, and the decrease is related objectively to an event occurring after the impairment was recognized, then in this case the impairment loss recognized in the past is reversed, in whole or in part, through income statement. The carrying amount of the investment in the asset at the date, on which the impairment loss is reversed, shall not exceed the amount of amortized cost of the asset which existed at that date if no impairment was previously recognized.
The impairment loss in respect of all the financial assets is reduced directly from the carrying amount of the financial asset, with the exception of trade and other receivables where the carrying amount is reduced through the use of an allowance account. When a trade receivable is uncollectible, it is written off against the allowance account. Collection in consecutive periods of amounts previously written off, are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in income statement.

r. Financial liabilities and equity instruments issued by the Group

Classification as a financial liability or an equity instrument:

Non-derivative financial instruments are classified as a financial liability or an equity instrument, in accordance with the nature of their contractual arrangements.

An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities. Equity instruments issued by the Group are recorded at the proceeds received, net of costs directly related to the issuance of these instruments.

Financial liabilities are presented and measured in accordance with the following classification:

- Financial liabilities at fair value through income statement.
- Other financial liabilities.

Note 2 – Significant accounting principles (cont.)

r. Financial liabilities and equity instruments issued by the Group (cont.)

Other financial liabilities:

Other financial liabilities are recognized initially at fair value after deducting transaction costs. After the initial recognition, other financial liabilities are measured at amortized cost using the effective interest method.

The effective interest method is a method of calculating the amortized cost of a financial liability and of allocating interest expenses over the relevant period. The effective interest rate is the rate that exactly discounts the flow of estimated future cash flows over the expected life of the financial liability to the carrying amount thereof, or, where appropriate, over a shorter period.

Derecognition of financial liabilities:

A financial liability is removed when, and only when, it is extinguished - that is, when the liability specified in the contract is either discharged, cancelled or expires.
Equity instruments issued by the Company in exchange for the removal of a financial liability are consideration paid against the settlement of the liability. Accordingly, the difference between the fair value of the equity instruments issued, and the carrying amount of the liability is recognized in income statement.

s. Derivative financial instruments for hedging purposes (hedging)

The Group sometimes carries out engagements in derivative financial instruments such as forward contracts and trading in foreign currency options in order to hedge itself against the risks connected with fluctuations in the rates of exchange of foreign currency. These financial derivatives are first recognized at fair value. After the initial recognition, the financial derivatives are measured at fair value. Derivatives are recognized in the consolidated balance sheets as assets when their fair value is positive and as liabilities when their fair value is negative.

Profits or losses resulting from changes in the fair value of derivatives which are not used for hedging purposes are immediately recorded to the statement of income.

Hedging transactions which meet the criteria of hedging transactions (hedging) are treated as follows:

Hedging fair value

A change in the fair value of the derivative (the hedging item) and the hedged item are recognized in the statement of income. In the events of hedging fair value which relates to the hedged item presented at amortized cost, the adjustments to the carrying amount in the financial statements are recognized in the statement of income over the remaining period until repayment. Adjustments to hedged financial instruments presented using the effective interest method, are recognized in the statement of income. When the hedged item is derecognized, the balance of the adjustments of fair value not yet amortized is recognized in the statement of income at that time.

Hedging cash flows

The effective part of a profit or a loss from the hedging instrument is recognized in equity as other comprehensive income (loss) while the ineffective part is immediately recognized in the statement of income.

Note 2 – Significant accounting principles (cont.)

s. Derivative financial instruments for hedging purposes (hedging) (cont.)

Hedging cash flows (cont.)

Other comprehensive income (loss) is transferred to the statement of income when the results of the hedging transaction are recorded to the statement of income; for example when the hedged revenue or expense is recognized in the statement of income or when a forecasted transaction occurs. When the hedged item is the cost of a non- financial asset or liability, this cost includes also the amount of the other relative comprehensive income (loss) which is transferred from shareholders' equity on the date of the recognition of the asset or liability.

In those cases where a forecasted transaction or a firm commitment are no longer expected to occur, the amounts recognized in shareholder' equity in the past, are transferred to the statement of income. Once the hedging instrument expires or is sold, terminated or exercised, or when it is no longer designated as a hedging instrument, the amounts recognized in shareholders' equity in the past, remain in shareholders' equity until the date on which the forecasted transaction or the firm commitment occur.

t. Fair value measurement

Fair value is the price that would have been received for selling an asset or the price that would have been paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Fair value measurement is based on the assumption that the transaction takes place in the principal market of the asset or liability, or in the absence of a principal market, in the most advantageous market.

The fair value of an asset or a liability is measured while using the assumptions that market participants would use while pricing the asset or liability, assuming that market participants operate for the benefit of their own economic interests.

Fair value measurement for a non-financial asset takes into account the ability of the market participant to produce economic benefits by using the asset in its highest and best use or by selling it to another market participant who would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate under the circumstances, and for which sufficient data is available to measure fair value, while maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.
All of the assets and liabilities that are measured at fair value or that a disclosure related to their fair value has been provided, are categorized within the fair value hierarchy, based on the lowest source of input significant to the measurement of the fair value as a whole:

Level 1:	Quoted prices (unadjusted) in an active market for identical assets or liabilities.
Level 2:	Data other than quoted prices included within Level 1 that are observable either directly or indirectly.
Level 3:	Data that are not based on observable market data (valuation techniques which use inputs that are not based on observable market data).

Note 2 – Significant accounting principles (cont.)

u. Treasury shares

The shares of the Company which are held by a subsidiary are measured at their acquisition cost and are presented as a deduction in shareholders' equity. Any profit or loss resulting from the acquisition, sell, issue or cancellation of treasury shares is recorded directly to shareholders' equity.

v. Provisions

A provision in accordance with IAS 37 is recognized when the Group has a present obligation (legal or implied) as a result of a past event and it is probable that economic resources will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The expense shall be recognized in the statement of income less the reimbursement of the expense.

The following are the types of provisions that have been included in the financial statements:

Legal claims

Provision for claims is recognized when the Group has a legal obligation in the present or an implied obligation as a result of a past event, and it is more likely than not that the Group will require its financial resources to settle the obligation and it can be estimated reliably.

Restructuring costs

Provisions for restructuring costs are recognized when the Group has formulated a detailed formal plan for restructuring, and has created a valid expectation among those affected by it for the execution of the plan by way of commencing the implementation of the plan or by way of giving notice to those affected by it.
The provision for restructuring costs includes the direct expenditures arising from it. As part of the provision the costs which are needed for the execution of the restructuring and which are unrelated to the Group's continuing operations, are included.

w. Liabilities for benefits to employees

The Group has several employee benefits:

1. Short-term employee benefits:

   Short-term employee benefits are benefits which are expected to be fully paid, up to 12 months after the end of the annual reporting period during which the employees provide the relating services. These benefits include salaries, leave pay, paid sick leave, paid annual leave and social security contributions and are recognized as expenses as the services are rendered. Liability for a cash grant is recognized when the Group has a legal or implied obligation to pay the aforesaid amount for a service that was provided by the employee in the past and the amount can be estimated in a reliable fashion.

2. Post-employment benefits

   The plans are usually fund by contributions to insurance companies and they are classified as defined contribution plans and defined benefit plans.

Note 2 – Significant accounting principles (cont.)

w. Liabilities for benefits to employees (cont.)

2. Post-employment benefits (cont.)

The Group in Israel has defined contribution plans pursuant to Section 14 of the Israeli Severance Pay Law under which the Group pays fixed contributions and without having legal or implied obligation to pay further contributions even if the fund does not hold sufficient amounts to pay all employee benefits relating to the employee service in the current period and prior periods.

Contributions in the defined contribution plan in respect of severance pay or compensation are recognized as an expense when contributed to the plan simultaneously with receiving the employee's services.
In addition, the Group also has a defined benefit plan with regard to severance pay pursuant to the Israeli Severance Pay Law. According to the Law, employees are entitled to severance pay upon dismissal or retirement. The liability in regards with termination of employment is determined using the actuarial value of the projected entitlement unit method. The actuarial calculation takes into account future salary increases and rates of employee turnover based on the estimated time of payment. The amounts are presented based on discounted expected future cash flows, at interest rates in accordance with the expected yield at the reporting date of index-linked high quality corporate bonds with maturity dates that are close to the liability period of the severance pay.

The Company makes current deposits in respect of its liabilities to pay severance pay to certain of its employees regularly in pension funds and insurance companies (hereinafter- “the plan’s assets"). The plan’s assets consist of assets held in eligible insurance policies. The plan’s assets are not available to the Group's own creditors and cannot be paid directly to the Group.

The liability for employee benefits which is presented in the balance sheet represents the present value of the defined contribution plan liability less the fair value of the plan’s assets.

Remeasurement of the liability net is recorded as other comprehensive income in the period in which they occur.

x. Share-based payment transactions

The Company's employees, directors and service providers are entitled to benefits in the form of share-based payment which are settled with equity instruments.

Transactions settled with equity instruments

The cost of transactions settled with equity instruments with employees, directors and service providers is measured at the fair value of the equity instruments on the granting date. Fair value is determined using an appropriate pricing model, for additional details see Note 21, as follows.

The cost of transactions to service providers is measured at the fair value on the date of granting, and thereafter, at the date of providing the service, it is revalued to fair value with the changes being recorded to the statement of income.

Note 2 – Significant accounting principles (cont.)

x. Share-based payment transactions (cont.)

Transactions settled with equity instruments (cont.)

The cost of transactions settled with equity instruments is recognized in the statement of income, together with a corresponding increase in equity, over the period in which the performance conditions exist, and ends on the date on which the relevant employees and directors become entitled to the benefit (hereinafter – "the vesting period"). The cumulative expense recognized for transactions settled with equity instruments on each reporting date until the vesting date, reflects the extent to which the vesting period has expired, and the Group's best estimate of the number of equity instruments that will ultimately vest. The charge or credit to the statement of income represents the change in cumulative expense recognized at the beginning and end of that reported period.

No expense is recognized for grants that do not ultimately vest, except for grants where vesting is dependent on market conditions, which are treated as grants which vested irrespective of whether the market conditions are met, provided that all other vesting conditions (service and/or performance) were fulfilled.

When the Company modifies the conditions of a grant settled with equity instruments, the additional expense is recognized in addition to the original expense that was calculated for any modification that increases the total fair value of the benefit granted or is otherwise beneficial to the employee or director according to the fair value on the modification date.

Cancellation of the grant settled with an equity instrument is handled as if it vested on the date of the cancellation and the expense not yet recognized for the grant is immediately recognized. Nevertheless, if the grant that was cancelled is replaced by a new grant which is designated as an alternative grant on the date on which it is granted, the cancelled grant and the new grant will both be handled as a change in the original grant as described above.

y. Earnings (loss) per share

Earnings (loss) per share are calculated by dividing the net income (loss) attributable to shareholders of the Company by the weighted average number of ordinary shares outstanding during the period.
Potential ordinary shares are included in the computation of diluted earnings per share only if they result in diluted earnings per share from continuing operations. Potential ordinary shares that have been converted during the period are included in diluted earnings per share only until the conversion date and from that date they are included in basic earnings per share.

Note 3 – The key estimates and assumptions in preparing the financial statements

While implementing the Group's accounting policies, as described in Note 2 above, the Company's management is required, in some cases, to exercise comprehensive accounting discretion concerning the accounting estimates and assumptions regarding the carrying amounts of assets and liabilities that are not necessarily available from other sources. The related estimates and assumptions are based on historical experience as well as other relevant factors. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed regularly by the management. Revisions to the accounting estimates are recognized only at the period of time in which a change in the estimate was carried out, provided that the change has an impact only on that period of time or are recognized at the aforementioned period of time and in future periods

Note 3 – The key estimates and assumptions in preparing the financial statements (cont.)

of time, provided that the change has an impact on both the current period and future periods.

The following are the key assumptions made in the financial statements concerning uncertainties on the balance sheet date, and the critical estimates computed by the Group and that a significant adjustment in the estimates and assumptions is likely to change the value of the assets and liabilities in the financial statements in the consecutive reporting year:

Impairment of fixed assets

The Company examines the need to record an impairment of the carrying amount of fixed assets whenever there are indications resulting from events or changes in circumstances which indicate that the carrying amount in the financial statements is not recoverable. In cases where the carrying amount of fixed assets in the financial statements exceeds their recoverable amount, the assets are reduced to their recoverable amount. The recoverable amount is the higher of the fair value less costs for sale and the value of its use. In evaluating the value of use, the expected cash flows are discounted according to the discounting rate before tax, which reflects the specific risks of every asset. For an asset that does not create independent cash flows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recorded to the statement of income in accordance with the nature of the item whose value declines.

Deferred tax assets

Deferred tax assets are recognized for carry forward tax losses and deductible temporary differences not yet utilized to the extent that it is probable that future taxable income will be available against which the losses could be utilized. The management's careful consideration is required to determine the amount of deferred tax assets that can be recognized, based upon the timing, the amount of future taxable income expected, its origin and the tax planning strategies.

Note 4 – New financial reporting standards, published interpretations and amendments to standards

Amendment to IAS 7 “Statement of Cash Flows” (Disclosure of Changes in Liabilities arising from Financing Activities)

The amendment states that it is required to provide disclosure of information that enables the users of the financial statements to evaluate the changes in liabilities arising from financing activities, whether changes relating to cash flows or changes not relating to cash flows.

The amendment shall be applied by way of prospective application for annual reporting periods beginning on January 1, 2017 or thereafter. Early adoption is permitted. On the initial application of the amendment it is not required to present comparative information.

a. IFRS 15 – “Revenue from Contracts with Customers”

The new standard sets out a comprehensive mechanism that regulates the accounting treatment of revenues arising from contracts with customers. The standard supersedes IAS 18 “Revenue” and IAS 11 “Construction Contracts” and the commentaries thereto. The core principle of the standard is that the recognition of revenue shall reflect the transfer of goods or services to customers in an amount that represents the economic benefits that the entity expects to receive in exchange for them. For this purpose, the standard stipulates that the revenue recognition shall take place when the entity transfers

Note 4 – New financial reporting standards, published interpretations and amendments to standards (cont.)

a. IFRS 15 – "Revenue from Contracts with Customers" (cont.)

to the customer the goods and/or services listed in the contract in such a manner that the customer obtains control of those goods or services.

The standard sets out a five-stage model for implementing this principal:

1. Identifying the contract (or contracts) with the customer.
2. Identifying the performance obligations in the contract.
3. Determining the transaction price.
4. Allocation of the transaction price to the performance obligation.
5. Recognizing revenue when the entity completes a performance obligation.

The Implementation of the model depends on the specific facts and circumstances of the contract and requires, occasionally, the exercise of extensive discretion.

In addition, the standard stipulates extensive disclosure requirements regarding contracts with customers, the significant estimates and changes therein which were used when applying the provisions of the standard, and this in order to allow the users of the financial statements to understand the nature, quantity, timing and reliability of revenue and cash flows arising from contracts with customers.

The standard shall take effect for annual reporting periods beginning on January 1, 2018 or thereafter. Early adoption is permitted. In general, the standard will be applied retroactively; however, entities will be allowed to choose certain adjustments in the framework of the transitional provisions of the standard with regard to the implementation thereof for previous reporting periods.

The Company has examined the estimated impact of standard IFRS 15 on its financial statements and according to its assessment it is not expected be material.

b. IFRS 9 – Financial Instruments

General:

International Financial Reporting Standard IFRS 9 (2014) "Financial Instruments" (hereinafter – "the standard") is the final standard of the financial Instruments project. The standard cancels the previous stages of IFRS 9 published in the years 2009, 2010 and 2013. The final standard includes directives for classifying and measuring financial assets which were amended regarding those published in the first stage in 2009, and, includes the directives for classifying and measuring financial liabilities as published in the second stage in 2010, it proposes a more updated model and based on principles regarding hedging accounting and presents a new model to examine a forecasted loss from an impairment in value as detailed as follows. In addition the standard cancels the interpretation of IFRIC 9 "Re-examination of embedded derivatives".

Financial assets

The standard establishes that the financial assets will be recognized and measured in the following manner:

- Debt instruments will be classified and measured after the initial recognition under one of the following alternatives: amortized cost, fair value through income

Note 4 – New financial reporting standards, published interpretations and amendments to standards (cont.)

b. IFRS 9 – Financial Instruments (cont.)

Financial assets (cont.)

statement or at fair value through other comprehensive income. Determining the measurement model shall be while taking into account the entity's business model regarding the management of financial assets and in accordance with the characteristics of the contractual cash flows arising from these financial assets.

- A debt instrument that according to the tests was measured at amortized cost or at fair value through other comprehensive income can be designated to fair value through the statements of income only when the designation cancels any inconsistency in the recognition and measurement that would have occurred if the asset was measured at amortized cost or at fair value through other comprehensive income.

- In general, equity instruments shall be measured at fair value through income statement.

- Equity instruments can be designated at the initial recognition to fair value through other comprehensive income. Instruments designated as aforesaid shall no longer be subject to examination for impairment and resulting profit or loss will not be transferred to income statement, including upon the realization.

- Embedded derivatives shall not be separated from a host contract covered by the standard. In lieu of this, hybrid contracts would be measured in their entirety at amortized cost or at fair value, in accordance with the business model tests and contractual cash flows.

- Debt instruments will be reclassified only when the entity changes its business model for managing financial assets.

- Investments in equity instruments without a quoted price in an active market including derivatives of these instruments shall be measured at fair value. The option to measure by cost under certain circumstances has been canceled. At the same time, the standard notes that under specific circumstances measurement by cost may be an appropriate estimate of fair value.

Financial liabilities

The standard also stipulates the following provisions concerning financial liabilities:

- The change in the fair value of a financial liability which is designated upon initial recognition at fair value through the statements of income, attributable to changes in credit risk of the liability, will be recorded directly to other comprehensive income unless it creates or increases accounting mismatch.

- When the financial liability is repaid or extinguished, amounts recorded to other comprehensive income will not be classified to income statement.

- All derivatives, whether assets or liabilities, will be measured at fair value through income statement, including a derivative financial instrument constituting a liability connected to an unquoted equity instrument the fair value of which cannot be measured reliably.

Note 4 – New financial reporting standards, published interpretations and amendments to standards (cont.)

b. IFRS 9 – Financial Instruments (cont.)

Impairment

The new model for impairment which is based on expected credit losses will be applied to debt instruments measured at amortized cost or at fair value through other comprehensive income, receivables in respect of lease, contract assets recognized under IFRS 15 and written obligations to provide loans and financial guarantee contracts.

The provision for impairment shall be for expected losses according to the probability of default in the following 12 months (next year), or according to the probability of default throughout the lifetime of the instrument (lifetime). Examination over the lifetime of the instrument is required if the credit risk has increased significantly from the initial recognition date of the asset. Another approach applies regarding purchased or originated credit-impaired financial assets.

The standard adds presentation guidelines and disclosure relating to the impairment of financial instruments.

Effective date and early adoption possibilities
This standard shall take effect for annual reporting periods beginning on January1, 2018, or thereafter. Earlier application is permitted.

In general, the standard's provisions regarding financial assets and liabilities shall be implemented retrospectively, with certain exceptions prescribed in the transitional provisions of the standard. It was also decided that despite the retroactive implementation, companies implementing the standard for the first time shall not be required to amend their comparison numbers for previous periods. Moreover, the comparison numbers can only be corrected when their correction makes no use of hindsight. Provisions referring to hedging shall be implemented, as a rule, on a prospective basis, with limited retrospective application.

The Company has examined the estimated impact of IFRS 9 on its financial statements and according to its assessment it is not expected be material.

c. IFRS 16 – Leases

The new standard which was issued in January 2016 replaces IAS 17 "leases" and the related interpretations, and sets out the principles for the recognition, measurement, presentation and disclosure of leases in relation to both parties of a transaction, meaning the customer ('lessee') and the supplier ('lessor').

The new standard eliminates the existing distinction regarding lessee, between finance leases and operating leases and provides a uniform accounting model in relation to all types of leases. In accordance with the new model, for every leased asset, the lessee is required to recognize the asset for right-of-use on the one hand, and on the other hand, the financial liability for the leasing fees.

The provisions for recognizing the asset and liability, as aforementioned, shall not apply in respect of assets leased for a period of up to 12 months and in relation to leases of low-value assets (for example, personal computers).

The standard does not change the current accounting treatment of the books of the lessor.

The standard shall take effect regarding annual reporting periods beginning on January 1, 2019 or thereafter. Early adoption is permitted, provided that IFRS 15 "Revenue from

Note 4 – New financial reporting standards, published interpretations and amendments to standards (cont.)

c. IFRS 16 – Leases (cont.)

Contracts with Customers" is also applied. In general, the standard will be applied retroactively; however entities will be allowed to choose certain adjustments in the framework of the transitional provisions of the standard with regard to the implementation thereof for previous reporting periods.

At this stage, the Company is evaluating the impact of the provisions of the standard on its financial statements. The principal expected effects, as estimated for the time being, are detailed as follows:

- An increase in the volume of assets and liabilities of the Company, due to the recording of all of the Company's lease transactions as right-of-use assets on the assets item, against a corresponding obligation to pay the lease fees in the liabilities item.
- The new standard also has an effect on the Company's statements of income. Whereas, according to the existing standard (IAS 17), the lease expenses are recognized on a straight line basis over the lease period, according to the new standard, the lease expenses will be recognized as a depreciation of the right of use of the asset and as financing expenses with the financial liability. In light of the fact that the effective interest method leads to recognition of higher expenses at the beginning of the lease period and lower expenses towards the end of the lease period, the aforementioned change in the timing of the recognition of such expenses is expected to affect the Company's results, which is currently being examined by the Company and will be quantified later.
- A decrease in the lease expenses currently included in the statement of income against an increase in depreciation and amortization expenses (depreciation of the right of use) and an increase in financing expenses due to the interest embedded in the liability to pay the lease fees, will result in a change in the Company's operating income.
- In accordance with the existing standard (IAS 17), the cash flows in respect of the Company's leases are classified as cash flows from operating activities. In accordance with the new standard, the lease fees constitute as a repayment of the financial liability towards the lessor, and therefore the standard is expected to result in an increase in cash flow from the Company's current operations, due to the classification of the principal and interest component in lease fees as cash flows for financing activities
- The Company has financial covenants, the compliance of which will not be affected by the implementation of the new standard, and it is not expected that the implementation of the standard will affect the Company's such engagements and others.

Note 5 - Trade receivables, net

	As at December 31, 2017	As at December 31, 2016
	Dollars thousands	
Open receivables	17,746	16,736
Checks for collection	1	58
	17,747	16,794
With deduction - provision for doubtful debts	(33)	(113)
Trade receivables, net	17,714	16,681

Out of the total balance of trade receivables as at December 31, 2017, approximately US 8.1 million dollars (2016: US 4.4 million dollars) are in respect of a debt of the customer Wal-Mart.

The Company has an agreement with a financial corporation in a factoring contract in respect of certain debts of its customers.
As at December 31, 2017, the total sum of debts for which a discount was carried out amounted to US 2.5 million dollars. As at December 31, 2016, a total sum of US 1.9 million dollars. The balance of trade receivable is shown net of the aforementioned amounts.

Trade receivables whose collection is in doubt are accounted for through recording a provision for doubtful debts.

The movement in the provision for doubtful debts is as follows:

	Dollars thousands
Balance as at January 1, 2016	208
Provision during the year	-
Amounts returned during the year	-
Recognition of written off doubtful debts	(95)
Balance as at December 31, 2016	113
Provision during the year	-
Amounts returned during the year	-
Amounts of written off doubtful debts	(80)
Balance as at December 31, 2017	33

The following is the analysis of the balances of trade receivables for which no impairment was recorded (provision for doubtful debts), trade receivables net, according to the period of delay in collection in relation to the reporting date:

	Trade receivables whose debts have not yet fallen due (no delay in collection)	Past due trade receivables and the delay in their collection is: Under 30 days	30 – 60 days	60 – 90 days	90 – 120 days	Over 120 days	Total
	Dollars thousands						
December 31, 2017	15,439	890	168	427	164	626	17,714
December 31, 2016	15,314	478	501	239	53	96	16,681

Note 6 - Other receivables

	December 31, 2017	December 31, 2016
	Dollars thousands	
Prepaid expenses	1,096	919
Advances to vendors	536	1,093
Institutions	944	942
Revenues receivable	17	571
Other receivables	651	604
	3,244	4,129

Note 7 - Inventories

	December 31, 2017	December 31, 2016
	Dollars thousands	
Raw Materials	2,043	3,340
Work in process	2,743	6,899
Finished goods	20,898	14,335
	25,684	24,574

(*) An impairment of slow inventory recognized as part of cost of sales amounted to 627 thousand dollars (2016 – 436 thousand dollars).

Tefron Ltd.

Notes to the Consolidated Financial Statements

Note 8 – Fixed assets

a. Composition and movement:

The year of 2017

	Land and buildings	Machinery and equipment (**)	Office furniture and equipment	Leasehold improve-ments	Total
	Dollars thousand				
Cost					
Balance as at January 1, 2017	3,863	126,826	2,898	7,461	141,048
Additions during the year	-	890	324	277	1,491
Balance as at December 31, 2017	3,863	127,716	3,222	7,738	142,539
Accumulated depreciation					
Balance as at January 1, 2017	1,724	(*)104,563	2,104	(*)5,660	114,051
Additions during the year	78	4,588	302	600	5,568
Balance as at December 31, 2017	,1802	109,151	2,406	6,260	119,619
Provision for impairment					
Balance as at January 1, 2017	470	2,055	124	-	2,649
Cancellation of provision for impairment	(351)	-	-	-	(351)
Amortization during the year	-	(846)	(86)	-	(932)
Balance as at December 31, 2017	119	1,209	38	-	1,366
Balance of amortized cost as at December 31, 2017	,1942	17,356	778	1,478	21,554

(*) Reclassified

(**) Machinery and equipment are presented net of investment grants.

Note 8 – Fixed assets (cont.)

a. Composition and movement

The year of 2016:

	Land and buildings	Machinery and equipment (*)	Office furniture and equipment	Leasehold improve-ments	Total
			Dollars thousand		
Cost					
Balance as at January 1, 2016	3,863	125,805	2,528	7,227	139,423
Additions during the year	-	1,021	370	234	1,625
Balance as at December 31, 2016	3,863	126,826	2,898	7,461	141,048
Accumulated depreciation					
Balance as at January 1, 2016	1,674	102,495	1,927	2,940	109,036
Additions during the year	50	4,217	177	571	5,015
Balance as at December 31, 2016	,1724	106,712	2,104	3,511	114,051
Provision for impairment					
Balance as at January 1, 2016	470	2,075	124	-	2,669
Amortization during the year	-	20	-	-	20
Balance as at December 31,2016	470	2,055	124	-	2,649
Balance of amortized cost as at December 31, 2016	,1669	18,059	670	3,950	24,348

(*) Machinery and equipment are presented net of investment grants.

b. Regarding liens, see Note 19d,

c. **Examining the recoverable amount of a cash-generating unit**

Due to the continuing losses of the brands segment, the Company performed a valuation of the recoverable amount of a cash-generating unit to which machinery and equipment and some improvements in leased property are attributed. The examination was performed as at December 31, 2017 by estimation of the net realizable value through valuation of the realization of property and machinery. To this valuation were added net operating assets that are financial assets and inventory which belong the unit, in accordance with the provisions of IAS 36. The valuation of the fixed assets, as aforementioned, was carried out by an external independent valuator. The valuation was carried out at fair value less sale costs. In accordance with the valuation as described above it was determined that no impairment is required.

Note 8 – Fixed assets (cont.)

d. Purchase of fixed assets on credit

In 2017 and 2016 the Company did not purchase fixed assets on credit. In 2015 the Company purchased fixed assets on credit on the sum of US 2,750 thousand dollars for a period of three years and nine months, so as of March 31, 2015 till September 30, 2018 the principal will be repaid and interest shall be paid.

Tefron Ltd.

Notes to the Consolidated Financial Statements

Note 9 - Other assets

a. Goodwill and intangible assets

The year of 2017

	List of customers	Goodwill	Total
	Dollars thousand		
Balance as at January 1, 2017	2,037	49	2,086
Additions during the year	-	-	-
Balance as at December 31, 2017	2,037	49	2,086
Accumulated amortization			
Balance as at January 1, 2017	1,873	-	1,873
Amortization recognized during the year	138	-	138
Balance as at December 31, 2017	2,011	-	2,011
Amortized balance as at December 31, 2017	26	49	75

The year of 2016

	List of customers	Goodwill	Total
	Dollars thousand		
Balance as at January 1, 2016	2,037	49	2,086
Additions during the year	-	-	-
Balance as at December 31, 2016	2,037	49	2,086
Accumulated amortization			
Balance as at January 1, 2016	1,782	-	1,782
Amortization recognized during the year	91	-	91
Balance as at December 31, 2016	1,873	-	1,873
Amortized balance as at December 31, 2016	164	49	213

The list of customers and goodwill were bought through business combinations. The customer list is amortized over a period of 8 years

Note 9 - Other assets (cont.)

b. Computer software

The year of 2017

	Computer software
	Dollars thousand
Cost	
Balance as at January 1, 2017	3,411
Additions during the year	411
Balance as at December 31, 2017	3,822
Accumulated amortization	
Balance as at January 1, 2017	2,044
Amortization recognized during the year	166
Balance as at December 31, 2017	2,210
Amortized balance as at December 31, 2017	1,612

The year of 2016

	Computer software
	Dollars thousand
Cost	
Balance as at January 1, 2016	3,144
Additions during the year	267
Balance as at December 31, 2016	3,411
Accumulated amortization	
Balance as at January 1, 2016	1,837
Amortization recognized during the year	171
Balance as at December 31, 2016	2,044
Amortized balance as at December 31, 2016	1,367

Note 10 - Credit from banks

a. Composition

	In NIS	Unlinked	Total
	Dollars thousands		
December 31, 2017			
Short-term credit from banks	914	11,621	12,535
Current maturities of long-term loans	-	1,650	1,650
	914	13,271	14,185
December 31, 2016			
Short-term credit from banks	876	12,630	13,506
Current maturities of long-term loans	-	1,650	1,650
	876	14,280	15,156

b. Regarding collateral and liens see Note 19d, as follows.

Note 11 - Trade payables

	As at December 31	
	2017	2016
	Dollars thousands	
Open accounts	16,446	17,341
Notes payable	5,408	557
	21,854	17,898

Note 12 - Other payables

	As at December 31	
	2017	2016
	Dollars thousands	
Liability to employees and other liabilities for wages and salaries	1,807	1,840
Accrued expenses	259	337
Institutions	70	369
	2,136	2,546

Note 13 - Long-term loans from banks and vendors

a. Composition:

As at December 31, 2017

	Nominal rate of interest	Balance	Balance less current maturities
	%	Dollars thousands	
Loans from banks	Libor + 4.5-5	10,852	9,202

As at December 31, 2016

	Nominal rate of interest	Balance	Balance less current maturities
	%	Dollars thousands	
Loans from banks	Libor + 3.9-5	12,476	10,826

b. Agreement with the banks regarding the reorganization of the credit lines

On March 2, 2010, the Company signed an agreement with its financing banks which included a reorganization of credit financing that the banks provide for the Company. The Company has adopted the provisions of IAS 39 (while examining the quantitative and qualitative criteria) and handled the new arrangement as an insignificant change in conditions. The agreement was amended on December 24, 2010, on December 27, 2011, on March 27, 2014 and on May 18, 2015 (hereinafter jointly: the "agreement").

The following is a summary of the main provisions of the signed agreement and the amendments thereto:

1. The long term credit line which was provided for the Company was divided into loans and credit lines as follows:

1.1 Long-term loans

The outstanding balance of the long-term loans from the banks on a total sum of 16 million dollars, as at January 1, 2015, was refinanced as a new loan for a period of eight years, when the principal of the loan will be repaid as follows: a sum of 1.7 million dollars was repaid in 2015, 1.65 million dollars will be repaid on each year as of 2016 till 2022 (inclusive) and a sum of 2.75 million dollars will be repaid in the first quarter of 2023.
The interest on the loans which shall be variable interest was determined with each of the banks and it will be paid quarterly.
It was determined in the agreement that in any event in which the Company will decide to sell an asset, not in the normal course of business, then the full net proceeds of the sale of the asset will serve for the purpose of early repayment.

As at December 31, 2017, the Company has long-term loans from banks in the amount of about US 10.9 million dollars. The Company is in compliance with all of the repayments of the loans as aforesaid.

1.2 Short-term credit lines

On June 11, 2015, the short-term credit lines were increased from a sum of US 9.75 million dollars to a sum of US 11.75 million dollars (hereinafter: the "base limit").

Note 13 - Long-term loans from banks and vendors (cont.)

b. Agreement with the banks regarding the reorganization of the credit lines (cont.)

1. The long term credit line which was provided for the Company was divided into loans and credit lines as follows (cont.):

1.2 Short-term credit lines (cont.)

The base limit might be increased by an additional amount of up to US 3.5 million dollars, depending on the sales of the Company, as detailed as follows:

a. On each quarter an examination of the Company's sales on a cumulative basis in the last four quarters will be carried out. As these sales shall exceed the sum of US 95 million dollars (hereinafter: the "base sales"), then the base limit shall increase by a sum equal to 30% of the sum of the increase in the sales which has exceeded the base sales. In any event the credit limit shall not exceed the sum of US 15.25 million dollars.

b. The aforementioned examination in Sub-clause a above, shall be carried out on a quarterly basis in comparison to the base sales, and as a result of such examination the credit limit might also be decreased in comparison to the previous quarter, as applicable. In any event, the credit limit, as a result of such a decrease, shall not be less than the base limit.

As at December 31, 2017, the short-term credit line at the banks in practice amounted to US 13.45 million dollars. As at December 31, 2017 all of the credit facilities have been utilized, through loans and short-term credit facilities. During 2017, the short-term credit facility at the banks decreased by US 1.3 million dollars, pursuant to the provisions of Clause 4.1 in this note as follows.

2. Factoring

In accordance with the agreement, the Company may carry out factoring transactions (liens and/or sale of customers' notes in favor of third parties to provide financing) whose total amount shall not exceed 4.5 million dollars and this provided that the short-term credit lines remain in effect.

3. Options to banks

In accordance with the provisions of the amendment to the agreement dated March 27, 2014, the Company issued to the banks, free of charge, a total of 300,000 option warrants, non- tradable and non-transferable, exercisable into ordinary shares of the Company of NIS 10 par value each, in accordance with the cashless mechanism against payment of an exercise price of US 2.5 dollars per share. The options shall be exercisable (in whole or in part) until December 31, 2019. On September 9, 2015, and in accordance with the provisions of the amendment to the financing agreement, the Company issued an amendment to the allocation letters that were given to the banks and according to which the terms of the options were amended in such a way that the exercise price of each option shall be US 1.43 dollars (instead of US 2.5 dollars), and the options shall be exercisable until March 31, 2023 (instead of December 31, 2019).

Furthermore, the terms of the options stipulate that in any case in which during the exercise period the Company's share price on the Tel Aviv Stock Exchange Ltd. shall be higher than an amount equal to US 3 dollars, the Company may require the banks to exercise the options and the banks are committed to do so immediately . For details, see Note 15 below.

Note 13 - Long-term loans from banks and vendors (cont.)

b. Agreement with the banks regarding the reorganization of the credit lines (cont.)

3. Options to banks (cont.)

It should be noted that according to the provisions of the agreement and its previous amendments, the Company issued to the banks, without charge, a total of 300,000 option warrants, which as at this date have expired, exercisable into 300,000 ordinary shares of the Company of NIS 10 par value each (1) 200,000 options allocated to the banks on October 11, 2011, expired on July 9, 2014, simultaneously with the grant of the new option warrants, (2) 100,000 option warrants which were allocated to the banks on August 17, 2010, which expired after 48 months passed and in accordance with the terms of the grant.

See also an event subsequent to the balance sheet date, dated March 22, 2018, Note 26a as follows.

4. Financial covenants

The following are details regarding the financial covenants (which will be calculated) according to the quarterly and annual financial reports of the Company, audited or reviewed (consolidated), as set out in the agreement.
The breach of each of the undertakings detailed as follows shall be considered as a breach of the financial ratios.
The banks may inform of a change in the financial covenants in the event of a change in accounting standards, and this without requiring the Company's consent.

4.1 The rate of tangible shareholders' equity of the total balance sheet will not be less than 30% at any given time; however, in any case, the tangible shareholders' will not be less than US 27.5 million dollars. In any event in which the tangible shareholders' equity shall be less than the aforementioned amount, however it shall not be less than US 25.5 million dollars, then it shall not constitute as a violation of the obligation detailed in this clause as long as Tefron shall decrease its credit limit, which is relevant to such a date (see Clause 1.2 (a)(b) above), in an amount equal to the difference between the sum of the tangible shareholders' equity and a sum of US 27.5 million dollars.

"Tangible shareholders' equity": The total issued and paid up share capital in addition with the capital reserves and the balance of the retained earnings, as well as the balance of the owners' loans for which subordination was signed to the banks by the Company and its shareholders, in addition to its liabilities for options that were granted and/or shall be granted to the banks, less intangible assets (such as goodwill, copyrights, patents, trademarks and trade names etc.), and less the treasury shares and receivables who are interested parties in the Company and/or its subsidiaries and/or related companies (as those are defined in the Securities Law- 1968).

4.2 The Company's balances of trade receivables, in accordance with the financial statements shall not be less at any given time than a sum of US 11.666 million dollars, plus a sum equal to one-third of the amount of the credit limit increase beyond the "base limit" (see Clause 1.2 above).

4.3 The Balance of cash, inventory and trade receivables – the total amount of the balances of the Company's cash, inventory and trade receivables shall not be less at any given time than a sum of US 32 million dollars plus an amount equal to the sum of the credit limit increase beyond the "base limit" (see Clause 1.2 above), or

Note 13 - Long-term loans from banks and vendors (cont.)

b. Agreement with the banks regarding the reorganization of the credit lines (cont.)

4. Financial covenants (cont.)

4.3 less the amount of the deduction of the credit limits from the base limit, in the event of a decline in the shareholders' equity below a sum of US 27.5 million dollars, as stated in Sub-clause 4.1 above.

4.4. The ratio between the Company's total debts and liabilities to the banks and other financial organizations and the Company's annual EBITDA according to the consolidated annual statements:

a) In 2013 – will not exceed 7.5
b) As of 2014 until 2017 (inclusive) – will not exceed 6.5.
c) As of 2018 and thereafter – will not exceed 5.5.

4.5 The current ratio (current assets divided by current liabilities) of the Company, according to its annual financial statements or quarterly reports, shall not be less than 1.2.

The breach of each of the undertakings to maintain the financial ratios detailed above (hereinafter: "the financial ratios"), will be considered as a breach of the financial ratios.

5. Additional provisions:

In addition to the detailed above, the Company has undertaken, amongst other things, the following additional obligations:

a. As long as the bank credit has not been repaid, the Company will not pay and not commit to pay dividends to its shareholders without receiving the written consent of the banks in advance;

b. No change shall be executed regarding the control of the Company in regards with the control structure, as it was upon the completion of the private placement (as detailed in Note 20a as follows), and this without receiving the agreement of the banks in advance and in writing. In spite of the aforementioned, a cumulative change whereas the holdings of the controlling shareholders as at the closing date, which shall not be less, at any given time, than 45% of the issued and paid up share capital of the Company, shall not constitute a violation of the obligations according to this clause;

c. Not to hold subsidiaries or other related companies, unless those companies shall sign a letter of commitment to the banks, unless the consent of the banks is granted.

d. Unless the banks grant their consent, Tefron Group shall not carry out investments in fixed assets, exceeding the sums detailed as follows, on a cumulative basis:

1. The investment amount invested in the Company in shareholders' equity in accordance with the private placement as detailed in Note 20a.

2. An amount exceeding, as of the beginning of 2015, the amount of the aggregate balance of the Company's EBITDA, less payments of principal and interest on loans and taxes paid, and starting as of 2018 (inclusive), an additional sum of 50% of the current maturities of the payments to the banks (principal and interest) of the consecutive year, shall be deducted each year of the said aggregate balance.

Note 13 - Long-term loans from banks and vendors (cont.)

b. Agreement with the banks regarding the reorganization of the credit lines (cont.)

5. Additional provisions: (cont.)

Investments, as aforementioned, shall also be subject to the following terms:

1. Every single investment during the course of the year, in an amount exceeding US 5 million dollars, will be subject to a prior examination carried out by the banks.
2. The aggregate investments during the course of one year shall not exceed a sum of US 7 million dollars.

As at December 31, 2017, the Company met the financial covenants that were determined in the amendment to the agreement with the banks. See also an event subsequent to the balance sheet date as at March 29, 2018, Note 26b.

Note 14 - Financial instruments

a. Classification of financial assets and financial liabilities

The financial assets and financial liabilities in the balance sheet are classified by groups of financial instruments pursuant to IAS 39, as follows:

	As at December 31, 2017	As at December 31, 2016
	Dollars thousands	
Financial assets		
Financial assets measured at amortized cost:		
Trade receivables	17,714	16,681
Loans and receivables	2,300	1,175
Long-term receivables	118	118
Total financial assets measured at amortized cost	20,132	17,856
Total financial assets	20,132	17,856
Total current financial assets	20,014	17,856
Total non-current financial assets	118	-
Financial liabilities		
Financial liabilities measured at amortized cost:		
Loans and short-term credit from banks	23,387	25,982
Subordinated loan from the shareholders	1,852	-
Trade payables	21,854	17,898
Payables	1,556	2,546
Total financial liabilities measured at amortized cost	48,649	46,426
Financial liabilities at fair value through statement of income:		
Liabilities for bank options	20	95
Total financial liabilities at fair value through the statement of income	20	95
Total financial liabilities	48,669	46,521
Total current financial liabilities	37,566	34,557
Total non-current financial liabilities	11,103	11,964

b. Financial risk factors

The Group's activities expose it to various financial risks such as market risks (including foreign exchange risk and interest rate risk), credit risk and liquidity risk. The Group's comprehensive risk management plan focuses on activities that reduce to a minimum any possible negative effects on the Group's financial performance. The Group utilizes derivative financial instruments in order to hedge certain exposures to risks.

The Board discusses the overall risk management principles, including the specific policy for certain risks such as foreign exchange risk, interest rate risk, credit risk and liquidity risk, and the use of derivative financial instruments and non-derivative financial instruments.

1. <u>Foreign currency risk</u>

The Group operates in a large number of countries and is exposed to foreign currency risk resulting from the exposure to different currencies, mainly the NIS and the Euro. Foreign

Note 14 - Financial instruments (cont.)

b. Financial risk factors (cont.)

1. Foreign currency risk (cont.)

exchange risk arises from future commercial transactions, recognized assets and liabilities denominated in a different currency from the functional and the reporting currency (US Dollar) of the Company. The finance department is responsible for managing the net position of each foreign currency by the use of forward contracts and currency options, according to the Company's hedging policy. In general, the management's policy is to hedge the forecasted payroll expenses denominated in NIS, payments in NIS to vendors and payments in Euro to vendors. The hedging level is examined each period, according to the market conditions and the Company's ability to provide collateral for hedging transactions. In 2017 no hedging transactions were carried out due to working capital limitation.

2. Credit risk

The Group has no significant concentrations of credit risk. The Group has a policy to ensure that the sales of its products are carried out to customers with an appropriate credit history

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 likely 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 level of their financial strength.

Terms of sale to customers

Management of customer credit risk is managed in accordance with the policy, procedures and controls of the Company with respect to the management of customer credit risk. The evaluation of the credit quality of a customer is based on performance analysis and credit rating of each customer, according to which credit terms are determined for each specific customer. Outstanding customer balances that have yet to be repaid are reviewed regularly and shipments to major customers are usually covered by credit insurance. It shall be noted that the sales to a material customer that are carried out through an interested party, are not insured.

The Company's revenues are mainly from customers in the USA and Canada. The Group monitors trade receivable debts on a regular basis, and the financial statements include provisions for doubtful debts which properly reflect, in the Company's opinion, the loss inherent in the debts whose collection is in doubt.

3. Interest risk

The Group is exposed to the risk of changes in market interest rates resulting from short-term and long-term loans that were received which bear adjustable interest rate (the loans are linked to the Libor and Prime base interest rate).

4. Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial liabilities on due dates. The responsibility for managing liquidity risk is handled by the Company’s

Note 14 - Financial instruments (cont.)

b. Financial risk factors (cont.)

4. Liquidity risk (cont.)

management which carries out a plan of managing financial and liquidity risks for the short, medium and long terms according to the Company's needs. The Company manages the liquidity risk by carrying out current financial forecasts.

The Company holds cash and other financial instruments with various financial institutions in Israel and in additional countries in which the Group operates. The Group's policy as a borrower of credit is operations that are subject to the limitations of the financing agreement with the banks.

As at December 31, 2017 the cash balance amounted to US 1,220 thousand dollars.

The table below presents the maturity profile of the Group's financial liabilities based on contractual undiscounted payments:

As at December 31, 2017

	Up to one year	1 to 2 years	2 to 3 years	3 to 4 years	4 to 5 years	Over 5 years	Total
	Dollars thousands						
Loans from banks	14,156	1,624	1,627	1,632	1,636	2,712	23,387
Subordinated loan from the shareholders	-	1,852	-	-	-	-	1,852
Trade payables	21,854	-	-	-	-	-	21,854
Other payables	1,556	-	-	-	-	-	1,556
	37,566	3,476	1,627	1,632	1,636	2,712	48,649

As at December 31, 2016

	Up to one year	1 to 2 years	2 to 3 years	3 to 4 years	4 to 5 years	Over 5 years	Total
	Dollars thousands						
Loans from banks	15,156	1,622	1,619	1,622	1,613	4,350	25,982
Trade payables	17,836	1,043	-	-	-	-	18,879
Other payables	4,809	-	-	-	-	-	4,809
	37,801	2,665	1,619	1,622	1,613	4,350	49,670

c. Fair Value

The carrying amount of cash, trade receivables, other receivables, short-term and long-term bank credit, short-term and long-term trade payables and other payables matches or approximates their fair value.

d. Classification of financial instruments by fair value levels:

The financial instruments presented in the balance sheet at fair value are grouped into classes with similar characteristics using the following fair value hierarchy which is determined based on the source of input used in measuring the fair value:

Note 14 - Financial instruments (cont.)

d. Classification of financial instruments by fair value levels (cont.):

Level 1 - Quoted prices (unadjusted) in active market for identical assets or liabilities.
Level 2 - Data other than quoted prices included within Level 1 that are observable either directly or indirectly.
Level 3 - Data that are not based on observable market data (valuation techniques which use inputs that are not based on observable market data).

December 31, 2017

	Level 2
	Dollars thousand
Liabilities for bank options	(20)
Total	(20)

December 31, 2016

	Level 2
	Dollars thousand
Liabilities for bank options	(95)
Total	(95)

e. Change in interest rates

A change in the interest rates of the financial liabilities as at December 31 would have increased (decreased) the shareholders' equity and the profit or loss in the amounts presented below. This analysis assumes that all other variables will remain constant and ignores tax effects.

	Sensitivity test to changes in interest rates	
	Profit (loss) from change	
	10% increase in interest	10% decrease in interest
	Dollars thousands	
2017	(48)	48
2016	(130)	130

f. Foreign currency risk

Foreign currency risk is the risk that fair value of future cash flows of a financial instrument will fluctuate due to changes in foreign exchange rates.
As at December 31, 2017, the Company has surplus of financial liabilities in NIS over financial assets in the amount of US 3,930 thousand dollars (as at December 31, 2016 – US 2,500 thousand dollars).

Changes in Dollar - NIS exchange rates as at December 31 would have increased (decreased) the shareholders' equity and profit or loss by the following amounts. This analysis assumes that all other variables are constant and ignores tax effects.

Note 14 - Financial instruments (cont.)

f. Foreign currency risk (cont.)

	Sensitivity test to changes in NIS exchange rates	
	Profit (loss) from change	
	10% increase in exchange rate	10% decrease in exchange rate
	Dollars thousands	
2017	393	(393)
2016	250	(250)

Sensitivity tests and principal work assumptions:

The selected changes in the relevant risk variables were determined based on the management's estimates as to reasonably possible changes in these risk variables.

The Company has performed sensitivity tests of principal market risk factors that are liable to affect its reported operating results or reported financial condition. The sensitivity tests present the profit or loss and/or change in shareholders' equity (before tax), in respect of each financial instrument for the relevant risk variable chosen for that instrument as at each reporting date. The test of risk factors was determined based on the materiality of the exposure of the operating results or financial condition of each risk with reference to the functional currency and assuming that all the other variables are constant.

The sensitivity test for long-term loans with variable interest was performed on the variable component of interest.

Note 15 - Liability for options to banks

On July 9, 2014 the Company issued 300,000 cashless option warrants to the lending banks exercisable into 300,000 shares, in accordance with the provisions of the amended re-organization of the credit lines agreement with the financing banks dated March 27, 2014. These options replace two series of 100,000 and 200,000 cashless option warrants which were allocated in March 2010 and December 2010, respectively.
On September 9, 2015, and in accordance with the provisions of the amended financing agreement as at May 18, 2015, the Company issued to the banks an amendment to the allocation letters that were granted to them, according to which the terms of the options were changed, in such a manner that the exercise price of each option shall be US 1.43 dollars (instead of US 2.5 dollars) and the exercise period of each option shall be until March 31, 2023 (instead of December 31, 2019).
The value of the benefits inherent in granting these options amounted to US 20 thousand dollars as at December 31, 2017, and was recorded as a liability for options to banks, against the recording of financing expenses. This liability is measured periodically, according to the option evaluation model. In 2017, the Company recorded financing income of US 75 thousand dollars as a result of the revaluation of the liability for the banks' options (2016 - financing expenses on the sum of US 95 thousand dollars). See also events subsequent to the balance sheet date, Note 26a.

Note 16 - Assets and liabilities for employee benefits

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

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

1. **Defined contribution plans**

   The provisions of Section 14 of the Severance Pay Law, 1963, apply to part of the severance pay payments, pursuant to which the fixed contributions paid by the Group into pension funds and/or policies of insurance companies, release the Group from any additional liability to employees for whom such contributions were made as aforementioned. These contributions as well as contributions for remuneration represent defined contribution plans.

	For the year ended December 31		
	2017	2016	2015
	Dollars thousands		
Expenses in respect of defined contribution plans	516	471	494

2. **Defined benefit plans**

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

Note 16 - Assets and liabilities for employee benefits (cont.)

Post-employment benefits (cont.)

2. Defined benefit plans (cont.)

a. Changes in the defined benefit plan's liabilities and in fair value of the plan's assets

The year of 2017

		Expenses recorded in the statements of income					Loss due to remeasurement in other comprehensive income							
	Balance as at January 1,	Cost of current service	Interest Expenses, net	Cost of past service and effect of clearing	Total expenses recognized in statement of income in the period	Payments from the plan	Return on plan's assets (excluding amounts recognized in interest expenses, net)	Actuarial loss due to changes in demographic assumptions	Actuarial loss due to changes in financial assumptions	Actuarial loss due to experience deviations	Total effect on other compreh-ensive income in the period	Effect of changes in the exchange rates of foreign currency	Contributions deposited by the employer	Balance as at December 31, 2017
Liabilities for defined benefit	951	66	35	31	132	324	-	2	(14)	253	241	104	-	1,104
Fair value of plan's assets	(154)	-	(4)	-	(4)	(35)	41	-	-	-	41	(15)	(7)	(104)
Liability (asset) net for defined benefit	797	66	31	31	128	289	41	2	(14)	253	282	89	(7)	1,000

Note 16 - Assets and liabilities for employee benefits (cont.)

Post-employment benefits (cont.)

2. Defined benefit plans (cont.)

a. Changes in the defined benefit plan's liabilities and in fair value of the plan's assets

The year of 2016

	Expenses recorded in the statements of income						Loss due to remeasurement in other comprehensive income							
	Balance as at January 1,	Cost of current service	Interest expenses net	Cost of past service and effect of clearing	Total expenses recognized in statement of income in the period	Payments from the plan	Return on plan's assets (excluding amounts recognized in interest expenses, net)	Actuarial loss due to changes in demographic assumptions	Actuarial loss due to changes in financial assumptions	Actuarial loss due to experience deviations	Total effect on other compreh-ensive income in the period	Effect of changes in the exchange rates of foreign currency	Contributions deposited by the employer	Balance as at December 31, 2016
Liabilities for defined benefit	953	64	29	-	93	119	-	-	(4)	27	23	(2)	-	938
Fair value of plan's assets	(191)	-	(4)	-	(4)	(36)	5	-	-	-	5	2	(2)	(154)
Liability (asset) net for defined benefit	762	64	25	-	89	80	5	-	(4)	27	28	-	(2)	797

Note 16 - Assets and liabilities for employee benefits (cont.)

Post-employment benefits (cont.)

2. Defined benefit plans (cont.)

b. Principal assumptions used in determining the defined benefit plan

	2017	2016
	%	%
Discount rate (1)	3.43%	4.2%
Expected salary increase rate	1%	2%

(1) The discount rate is based on index-linked high quality corporate bonds.

c. Amounts, timing and uncertainties of future cash flows

The following are possible changes which are considered reasonable for the end of the reporting period, for each actuarial assumption, assuming that the remaining actuarial assumptions have remained unchanged:

	The change in the defined benefit obligation
	Dollars thousand
As at December 31, 2017:	
Sensitivity test to changes in expected salary increase rate	
The change as a result of:	
Salary increase of 1%	92
Salary decrease of 1%	(80)
Sensitivity test to changes in the discount rate of the plan's liabilities and assets	
The change as a result of:	
1% increase of the discount rate	(78)
1% decrease of the discount rate	91

Note 17 - Taxes on income

a. Tax laws applicable to the Group's companies

The Company is subject to provisions of Income Tax Regulations (Rules for Bookkeeping by Foreign Investment Companies and Certain Partnerships and Determination of Taxable Income), 1986. In accordance with the aforementioned regulations, the Company files its income tax returns in US dollars.

Impact of the U.S. Tax Reform

On December 22, 2017, the president of the United States, Donald Trump signed a legislation that would lead to major changes in the US tax laws (hereinafter: the "reform"), In the framework of the reform, significant changes have been carried out in the US tax laws, including some provisions that would have an impact on the Company's tax liability in the United States.

Note 17 - Taxes on income (cont.)

Impact of the U.S. Tax Reform (cont.)

The main provisions of the reform that are relevant to the Company are as follows:

1. Reducing the federal corporate tax rate from 35% to 21%, effective as of January 1, 2018.

2. Eliminating the minimum alternative tax (AMT) in respect of US companies and limiting the new net operating loss (loss incurred as of 1.1.2018) to 80% of the taxable income.

3. Imposing a one-time taxation on the cumulative net profit of controlled foreign companies (CFC) held at a rate of more than 50% by American shareholders (when each of them holds 10% or more of the company's shares). The effective tax rate imposed on these profits will be 15.5% in respect of cash and cash equivalents and 8% in respect of profits invested in non-liquid fixed assets, according to the balance of earnings measured as of November 2, 2017 or December 31, 2017, whichever is higher. The tax payment can be deployed over a period of up to 8 years.

4. Global Intangible Law - Taxed Income (GILTI) - excess income of controlled foreign companies (CFC) exceeding 10% of the return on tangible assets of the same CFC and other income taxed in the US under the CFC regulations, shall be subject to the US federal corporate tax at 10.5% tax rate until 2025 and 13.125% tax rate thereafter. In addition, and subject to certain conditions, it will be possible to receive a credit against 80% of the taxes paid in the foreign country.

5. Foreign Derived Intangible Income (FDII) – it is possible to receive a deduction for tax purposes (meaning reduced tax rate) in respect of certain income of the Company from exporting products or services, under certain conditions.

6. Interest expenses - according to the new legislation, during the years 2018 and up to 2021 (inclusive), companies will not be allowed to deduct interest expenses which amount to more than 30% of the total adjusted taxable income EBITDA of those companies. After 2021, interest expenses exceeding -30% of the total EBIT income of such companies will not be allowed to be deducted. Any amount not deductible during that year will be carried over to the following years on the basis of the same mechanism and without limitation in time.

7. Bonus Depreciation - an immediate accelerated depreciation at a certain rate of the cost of certain fixed assets which were placed in service between September 27, 2017 and January 1, 2026.

The reform is not expected to have a material impact on the Company's financial statements as at December 31, 2017.

Note 17 - Taxes on income (cont.)

b. Tax rates applicable to the Group:

In the beginning of January 2016, the Law for the Amendment of the Israeli Tax Ordinance was published, according to which the corporate income tax rate will be reduced to 25% (instead of 26.5%). The new corporate income tax rate will apply to income that was generated or accrued as of January 1, 2016. On December 29, 2016, the Economic Efficiency Law (Amendments to Legislation for the Achievement of the Budget targets for the 2017 and 2018 Budget Years) 2016, in the framework of which the following tax changes were determined:

The corporate tax rate will be reduced from 25% to 24% in 2017 on income generated or accrued as of January 1, 2017 and will continue to be reduced to 23% in 2018 and thereafter on income generated or accrued as of January 1, 2018.
The tax rate on a subsidiary in the United States as of January 1, 2018 is 21%.
The tax rate on a subsidiary in Canada is 24%.

El-Masira is incorporated in the Free Trade Zone in Jordan, and is taxed according to tax laws applicable in Jordan; the statutory tax rate in the Free Trade Zone in Jordan, for the industry in which the Group is engaged is 0%.

c. Final tax assessments

Final tax assessments were issued to the Company up to and including the tax year 2015. For the subsidiary Hi-Tex and the company Tefron-Macro which operate in Israel, have final tax assessments up to and including the tax year of 2011. The main subsidiary operating outside Israel has final tax assessments until the tax year of 2012.

d. Carry- forward losses for tax purposes and other temporary differences

In continuation of Note 25v regarding the merger between the Company and the subsidiary Hi-Tex, the merged company has carry-forward losses for tax purposes amounting to, as at December 31, 2017 a sum of US 43 million dollars which may be used over an unlimited period of time, and subject to the merger's limitations as specified in Note 25v as follows.
In respect of these balances and other deductible temporary differences, the Company recorded in its financial statements deferred tax assets on the sum of US 3 million dollars (due to their expected utilization as a result of the expected profit forecast for the next years and of the reserves for deferred taxes on the sum of US 4 million dollars, mainly for fixed assets, and the expectation of realizing them against taxable income). Another subsidiary Tefron-Macro has carry-forward losses for tax purposes in the sum of US 8 million dollars for which no deferred taxes have been accumulated since they are not expected to be utilized in the foreseeable future. A subsidiary which is registered in the United States, Tefron USA, has carry-forward losses for tax purposes on the sum of US 9 million dollars, for which no deferred taxes have been accumulated for reasons of immateriality. The utilization of the carry forward losses of Tefron USA is subject to restrictions as to the period in which it will be possible to utilize the losses in the future and as to the amount the Company could utilize each year.

Note 17 - Taxes on income (cont.)

e. Deferred taxes

Composition:

	Balance sheets		Statements of income		
	December 31		The year ended December 31		
	2017	2016	2017	2016	2015
	Dollars thousands				
Deferred tax liabilities					
Fixed assets	(3,585)	(4,182)	597	(2,433)	91
	(3,585)	(4,182)			
Deferred tax assets					
Carry-forward losses for tax purposes	6,128	6,836	(708)	1,976	(94)
Provision for doubtful accounts	-	16	(16)	-	-
Employee benefits	347	220	127	117	3
	6,475	7,072			
Deferred tax income (expenses)			-	(340)	-
Deferred tax assets, net	2,890	2,890			

Deferred taxes are presented in the balance sheet as follows:

	December 31	
	2017	2016
	Dollars thousands	
Non-current assets	2,890	2,890

Taxes on income relating to other comprehensive income items

	For the year ended December 31		
	2017	2016	2015
	Dollars thousands		
Loss from investment in securities available for sale	-	-	(35)

Note 17 - Taxes on income (cont.)

f. Tax to be paid (tax benefit) included in statement of income

	For the year ended December 31		
	2017	**2016**	**2015**
	Dollars thousands		
Current tax expenses	211	-	-
Expenses (income) in respect of taxes from previous years	(130)	442	-
Deferred taxes	-	340	-
	81	782	-

The Company does not intend to distribute dividends resulting from its industrial plant in a manner which would create an additional tax liability.

g. Theoretical tax

The reconciliation between the theoretical tax rate that would have applied 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 the statement of income, is as follows:

	For the year ended December 31		
	2017	**2016**	**2015**
	Dollars thousands		
Loss before taxes on income	(3,118)	(339)	(3,908)
Statutory tax rate	24%	25%	26.5%
Tax expenses (income) computed at the statutory tax rate	(748)	(85)	(1,036)
Increase (decrease) in taxes on income resulting from the following factors:			
Non-deductible expenses for tax purposes	12	25	38
Temporary differences for which no deferred taxes were recorded	1,034	1,204	59
Income subject to special tax rates	(12)	(1,173)	921
Adjustments carried out during the year in respect of taxes from previous years	(130)	442	-
Adjustments to deferred tax balances due to changes in tax rates	-	397	-
Others	(75)	(28)	17
Tax expenses (revenues)	81	782	-

Note 18 - Long-term payables

	December 31	
	2017	**2016**
	Dollars thousands	
Vendor credit – purchase of fixed assets (1)	-	1,043
	-	1,043

(1) For additional details see Note 8d above.

Note 19 - Contingent liabilities, commitments and liens

a. Contingent liabilities

1. In accordance to the Law for the Encouragement of Capital Investments, 1959, the Company and its subsidiary received in the past grants from the State of Israel according to their investments in enterprises. The receiving of the grants is conditional on implementing all of the conditions in the application for an approved enterprise status and furthermore on the fact that at least 30% of the investments will be financed by outstanding share capital. Lack of implementing the conditions in such application will result in the return of the grants with an addition of interest and linkage differences as of the date of their grant. The Company met the conditions determined by the Investment Center in all matters related to the receipt

2. Legal proceedings

On November 23, 2016, the Company reported that an indictment was submitted to the Labor Court against the Company's subsidiary, the Company's former CEO and a former employee of the subsidiary, claiming that the defendants have violated the workplace safety regulations in connection with a work accident, which occurred at the subsidiary in 2013. On April 7, 2017, the Company reached a plea bargain concerning the said indictment, which was approved by the Court, and according to which the former CEO of the Company was deleted from the indictment, the Company's subsidiary was fined NIS 15,000 and the former employee was fined NIS10,000.

b. Commitments

1. Engagement in an agreement for strategic cooperation in China

On November 12, 2014, the Company entered into an agreement with a company incorporated in China, who operates in the apparel field of seamless technology and serves as a subcontractor of the Company in China, for the purpose of strategic cooperation in China in the field of production and development of seamless apparel, the core business of the Company (hereinafter: “the cooperation”, “the agreement"). It should be noted that the Company is using several subcontractors in China on a regular basis. However, the purpose of this cooperation, as opposed to the operations with other subcontractors in China, is to allow the subcontractor with whom the Company entered into the said agreement, to produce products in the field of seamless products, using technology, that to the best knowledge of the Company, currently does not exist in China, and which the Company intends to teach the subcontractor while using means of protection against the usage of this technology by the subcontractor in favor of third parties. The purpose of the subcontractor’s usage of the said technology is to provide a marketing advantage for the Company with its customers who are interested in products made by this technology in China.

Note 19 - Contingent liabilities, commitments and liens (cont.)

b. Commitments (cont.)

2. Engagement in a joint venture agreement with Clover Group International Limited

On June 20, 2014, the Company engaged in a joint venture agreement (hereinafter: “the agreement") with Clover Group International Limited, a company incorporated in Hong Kong, specializing in the development, design and manufacturing of bras (hereinafter: "Clover") (hereinafter: “the parties"). In accordance with the agreement, utilizing the knowledge and experience of the Company in developing and manufacturing products using the seamless technology, and in conjunction with the knowledge and experience of Clover which is considered to be a leading company in the field of developing and manufacturing of bras, the parties will operate to establish a jointly owned company, in equal shares, in Hong Kong, whose main goal is designing, developing, manufacturing and selling bras produced by means of the seamless technology as well as other apparel products produced by means of this technology. In the framework of the agreement, arrangements were determined regarding the management of the company and with regard to the rights and obligations of the parties as shareholders in it, which naturally, due to the fact that the parties hold equal shares in the company, these arrangements are based on an agreement between the parties. In addition, the agreement includes provisions to regulate disagreement as well as provisions regarding the right of first refusal and the right to participate in the sale of shares as well as provisions relating to non-competition.

3. Extending the service agreement with a related party for invoicing services

On March 29, 2018, the Company’s Board approved the extension of the term of the agreement for providing invoicing services with Lamour Global Inc. Limited (hereinafter: “Lamour”), a private company incorporated in Canada who is amongst the controlling shareholders of the Company, in a non-extraordinary transaction, for an additional period of 3 years. Lamour shall serve as a channel for the sale of the Company’s products to Wal-Mart as detailed in Note 25g as follows. The Board's approval was obtained after receiving the recommendation of the Audit Committee according to which the extension of the period, as aforesaid, is reasonable under the circumstances.

c. Commitments to pay rent

The Company's plants and installations and most of those of its subsidiaries are located in buildings leased for various terms ending during the years 2018 - 2021.

The future minimum rent commitments under non-cancelable leases as at December 31 are as follows:

	2017	2016
	Dollars thousands	
Year 1	1,995	1,450
Year 2	1,644	1,395
Year 3	-	1,395
	3,639	4,240

As at the date of the report, the leased space was reduced- the liability is presented net of the leased space that was returned to the property owner. Furthermore, the Company also entered into lease agreements with a number of third parties to whom it has sub-leased part of the spaces for which it has a liability as mentioned above.

Note 19 - Contingent liabilities, commitments and liens (cont.)

d. Liens

1. All liabilities to banks are secured by a floating charge on the existing and future assets of the Company and its subsidiaries in both the present and the future.

2. To secure compliance with the conditions of the application for an "approved enterprise" status granted to the Company and its subsidiaries pursuant to the Law for the Encouragement of Capital Investments, 1959, the Company and its subsidiaries have pledged floating charges for an unlimited amount on all their assets in favor of the State of Israel.

Note 20 - Capital

a. Private Placement

On February 17, 2015, after obtaining the approval of the Audit Committee and Board, the Company signed an agreement with Litef Holdings Inc., a private company incorporated in Canada, who is among the controlling shareholders of the Company (hereinafter: "Litef"), according to which, Litef will invest a total of US 5 million dollars in the Company against an extraordinary private placement of 4,672,897 ordinary shares of the Company of NIS 10 par value each (hereinafter: “ordinary shares”) (hereinafter: “the agreement”), as detailed as follows.

On April 2, 2015, and pursuant to receiving the approval of the Company's Audit Committee and Board of Directors, the Company signed an agreement with Mazouz and Weisselberger Genesis Investment, Limited Partnership, Mr. Erez Rozenbuch and Mr. Tomer Hefetz (hereinafter: the "additional investors"), according to which each of the additional investors shall invest in the Company a sum of US 175 thousand dollars, and in total a sum of US 525 thousand dollars, against a private placement of 163,551 ordinary shares of the Company to each of the additional investors, and in total 490,653 ordinary shares (hereinafter: the "additional investment agreement"), furthermore the Company signed an amendment to the agreement resulting from the additional investment agreement (hereinafter the agreement and the additional investment agreement shall be called together: the “private placement").

At the eve of the allocation of shares, Litef and Nouvelle Intimes Seamless Inc., a private company incorporated in Canada (hereinafter: "Nouvelle") (Litef and Nouvelle shall be called hereinafter together: "Nouvelle Group") jointly held approximately 32.47% of the issued and paid up share capital of the Company and the voting rights therein and approximately 28.53% of the issued and paid up share capital of the Company and the voting rights therein on a fully diluted basis.

The principals of the agreement and the additional investment agreement are detailed as follows:

The principals of the agreement:

1. On the closing date (as this term is defined as follows) Litef shall invest a total of US 5 million dollars (hereinafter: the "investment amount") against an allocation of 4,672,897 ordinary shares of the Company, so that Litef shall pay a price of US 1.07 dollars per share.
   Upon the closing of the transaction, the Nouvelle Group shall jointly hold approximately 57.71% of the issued and paid up share capital of the Company and the voting rights therein and approximately 53.53% of the issued and paid up share capital of the Company and the voting rights therein on a fully diluted basis.

Note 20 - Capital (cont.)

a. Private Placement (cont.)

2. Nouvelle and Messrs. Ben and Martin Lieberman, who are amongst the controlling shareholders of the Company, signed on December 30, 2010, a commitment not to compete with the Company in the field of seamless products for a limited period of 5 years as of the date of signing such non-competition letter of commitment. In the framework of the agreement it was agreed upon that Litef would join as a party to the letter of commitment regarding the non-competition, and it will remain in force as long as Nouvelle, Messrs. Ben and Martin Lieberman, and Litef, each on its own, are amongst the controlling shareholders of the Company.

3. The closing of the transaction was set to a date no later than five business days after the existence of all the conditions precedent (hereinafter: "closing date") specified in the contract, including:

    a. The approval of the Stock Exchange regarding the registration for trading of the shares to be allocated under the agreement.

    b. The Company's engagement with its financing banks, Bank Leumi Le-Israel Ltd., Bank Hapoalim Ltd. and Israel Discount Bank Ltd. (hereinafter: the "banks") in an agreement to amend the existing financing agreement of the Company.

On May 18, 2015, the Company and its subsidiaries, Macro Clothing Ltd and Hi-Tex founded by Tefron Ltd., engaged in an amendment to the financing agreement with the banks which allows the existence of all the conditions precedent. For details see note 13b as follows.

The principals of the additional investment agreement:

As aforementioned, on April 2, 2015, the Company signed an additional investment agreement. According to this agreement on the closing date each of the additional investors shall invest a sum of US 175 thousand dollars, and in total a sum of US 525 thousand dollars, against an allocation of 490,653 of the Company's ordinary shares (163,551 ordinary shares to each of the additional investors), so that for each share the additional investors shall pay a sum of US 1.07 dollars.

The closing of the additional investment agreement has been set to the closing date of the transaction with Litef, and in any event, no later than May 31, 2015 or a postponed date as shall be agreed upon by the Company and Litef (provided that as long as the closing date shall be postponed to a date later than August 31, 2015, then the other investors will have the right to terminate the agreement), and all of the above subsequent to the fulfillment of all the conditions precedent as specified in the agreement, including:

a. An approval, in accordance with any law, for the private placement, including an approval for the allocation of the shares in accordance with the agreement and the additional investment agreement, by the Company’s Audit Committee and Board of Directors (that granted their approval at their meetings dated February 18, 2015, and April 1, 2015) and the approval of the general meeting of the Company’s shareholders (that granted its approval at its meeting dated May 25, 2015).
b. The approval of the Stock Exchange regarding the registration for trading of the shares to be allocated under the agreement (that was granted on May 27, 2015).
c. The closing of the transaction according to the agreement.

On May 25, 2015, a special meeting of the shareholders of the Company approved the Company’s engagement in the agreement, which includes a transaction between the Company and Litef and the additional investors, as well as the allocation of shares to Litef and the additional investors, as aforesaid.

On June 1, 2015, the shares were allocated in return of the consideration received.

Note 20 - Capital (cont.)

b. Composition of the share capital and the convertible securities

	As at December 31,	
	2017	**2016**
	Number of shares	
Authorized share capital (ordinary shares of NIS 10 par value each)	20,000,000	20,000,000
Issued share capital (ordinary shares of NIS 10 par value each)	11,970,026	11,970,026
Paid up share capital (ordinary shares of NIS 10 par value each)	11,870,286	11,870,286
Option warrants (non-tradable) for the Company's employees and managers, directors and service providers exercisable into ordinary shares of NIS 10 par value each	464,605	464,605
Rights to shares	-	135,000
treasury shares held by a subsidiary	99,740	99,740

c. Rights conferred by the shares

Ordinary shares

Voting rights at the general meeting, right to dividends, rights upon liquidation of the Company and the right to appoint directors of the Company.

d. Treasury shares

Tefron Holdings (98) Ltd., a wholly-owned subsidiary of the Company, holds 99,740 Company shares, which constitute 0.83% of the Company's shares and whose cost US 7,408 thousand dollars, as at December 31, 2017 and 2016. The investment in these shares is recorded according to the "treasury shares" method in the shareholders equity.

The shares are pledged in favor of the bank to secure a loan that was received.

e. Capital management in the Company

The Company's capital management objectives are:

1. To preserve the Group's ability to ensure business continuity thereby creating a return for the shareholders, investors and other interested parties.
2. To ensure adequate return for the shareholders by pricing products and services commensurately with the level of risk in the Group's business operations.

The Company operates to achieve a return on capital at a level that is customary in the industry and markets in which the Company operates. This return is subject to changes depending on market factors in the Company's industry and business environment. The Company is required to have minimum tangible equity of US 25.5 million dollars, as defined in the amendment to the agreement with the banks as described in Note 13b above, in the framework of the financial covenants included in the agreements with the banks in connection with providing loans, and is not subject to any demands relating to achieving a certain return on capital. In 2017, 2016 and 2015 the Company had a negative return on capital.

Note 21 - Share-based payment transactions

a. Expense recognized in the financial statements

The expense recognized in the Company's financial statements for services rendered by employees, directors and consultants is presented in the following table:

	For the year ended December 31		
	2017	2016	2015
	Dollars thousands		
Share based payment plans settled with equity instruments for employees and directors	-	12	36
Total share based payment plans settled with equity instruments	-	12	36

b. Share-based payment plan to the Company's employees and managers, directors and service providers

1. Option plan to the managers and employees of the Company

The share-based payment transactions the Company provided to its employees are described as follows.
On December 30, 2013, the general meeting of the shareholders of the Company approved the option plan for employees, officers and consultants. The option warrants shall vest and become exercisable and the offeree's eligibility to those warrants shall expire according to the following:

- One-third of the options (hereinafter: "the first series") will be exercisable beginning one year from the date of their allocation and until the end of five years as of the date on which the options included in the first series were first exercisable.
- One-third of the options (hereinafter: "the second series") will be exercisable beginning two years from the date of their allocation and until the end of five years as of the date on which the options included in the second series were first exercisable.
- One-third of the options (hereinafter: "the third series") will be exercisable beginning three years from the date of their allocation and until the end of five years as of the date on which the options included in the third series were first exercisable

This plan replaces the option plan which was approved in September 1997, and was extended once more in March 2008.

2. On November 21, 2013, the Company's Board of Directors granted to the Company's former CEO 150,000 option warrants exercisable to ordinary shares of the Company of NIS 10 par value each, in accordance with the cashless mechanism. The exercise price per option is US 2.22 dollars, after being translated to NIS at the representative rate of exchange of the US dollar on the day prior to the date of granting the options. Entitlement to realize the options will accrue over a period of three years as of the day of the allocation, in accordance with the Company's option plan.
The value of the benefits included in granting these options according to the share price on the date of trading on the Stock Exchange amounted to US 108 thousand dollars. On July 30, 2017, following the resignation of the CEO the aforementioned optioned expired.

Note 21 - Share-based payment transactions (cont.)

c. Movement during the year

The following table lists the number of share options, the weighted average exercise price of the share options, and modifications in employee option plans which were carried out during the current year:

	As at December 31, 2017		As at December 31, 2016	
	Number of share options	Weighted average exercise price (dollar)	Number of share options	Weighted average exercise price (dollar)
Options for shares granted at the beginning of the year	614,605	2.1	753,605	2.1
Options for shares granted during the year	-	-	-	-
Options for shares forfeited or expired during the year	(150,000)	-	(4,000)	-
Options for shares expired during the year	-	-	(135,000)	-
Options for shares exercised during the year	-	-	-	-
Options for shares at the end of the year	464,605	2.0	614,605	2.1
Options for shares which can be exercised at the end of the year	464,605	2.0	607,383	2.0

d. The weighted average of the remaining contractual term of the share options as at December 31, 2017 is 4.6 years (2016 – 4.4 years).

e. Measurement of the fair value of the share options settled with equity instruments

The Company uses the Black & Scholes model to measure the fair value of options to shares settled with equity instruments that have been granted to employees. The measurement is carried out on the date of granting the options for shares which are settled with equity instruments. The Company uses the Monte Carlo simulation method for measuring the fair value of the options granted to the banks. The measurement is carried out on the date of granting the options and a remeasurement is conducted quarterly.

The expected lifespan of the share options is based on the Company's historical data which is not necessarily indicative of the future exercise pattern of share options.

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

Tefron Ltd.

Notes to the Consolidated Financial Statements

Note 22 - Supplementary information to the statement of income items

a. Cost of sales

	For the year ended December 31		
	2017	**2016**	**2015**
	Dollars thousands		
Materials	72,205	72,575	53,242
Payroll and benefits	8,938	8,096	7,393
Sub-contracted work	10,635	7,265	6,225
Depreciation	4,457	4,744	4,363
Other manufacturing expenses	5,275	5,967	6,220
	101,510	98,647	77,443
Decrease (increase) in work-in-progress and finished goods inventories (*)	(2,407)	(6,116)	(2,861)
	99,103	92,531	74,582
(*) Including provision for impairment of slow inventory	627	436	433

b. Development expenses, net

	For the ended December 31		
	2017	**2016**	**2014**
	Dollars thousands		
Payroll and benefits	3,048	2,639	2,390
Manufacturing expenses	720	720	715
Depreciation and amortization	240	240	240
Materials	351	314	234
Others	109	78	115
	4,468	3,991	3,694

c. Selling and marketing expenses, net

	For the ended December 31		
	2017	**2016**	**2015**
	Dollars thousands		
Payroll and benefits	4,267	3,825	3,653
Transport, export and distribution	4,788	4,655	4,635
Commissions to agents and franchisees	4,029	3,166	2,651
Overseas office maintenance	466	255	234
Overseas excursions	1,076	831	786
Depreciation and amortization	243	271	295
Others	610	398	506
	15,479	13,401	12,760

Note 22 - Supplementary information to the statement of income items (cont.)

d. General and administrative expenses

	For the year ended December 31		
	2017	**2016**	**2015**
	Dollars thousands		
Payroll and benefits	1,232	1,030	1,242
Consulting	670	814	690
Remuneration and directors' insurance	291	288	347
Provision for doubtful and bad debts	-	14	(15)
Others	792	909	650
	2,985	3,055	2,914

e. Other expenses (income)

	For the year ended		
	2017	**2016**	**2015**
	Dollars thousands		
Reorganization (1)	120	1,128	817
Other income	(4)	(29)	-
Gains from canceling a provision for impairment (2)	(351)	-	-
	(235)	1,099	817

(1) In 2016 and 2015 the Company included in its reports restructuring costs on a total sum of US 1,128 thousand dollars, which resulted from executing the Company's plan for the relocation of the dyeing operation which is carried out by a subcontractor in Israel to a number of other subcontractors in Jordan. This was carried out as part of the risk management policy of the Company to reduce its dependence on a material supplier and to enable the Company operational flexibility. The restructuring costs include the costs of the relocation of the dyeing plant as well as the costs related to the termination of employer-employee relations.
In 2017, the Company included in its financial statements restructuring expenses in respect of the merger of the subsidiary Hi-Tex with and into the Company. For additional details regarding the merger, see Note 25v as follows.

(2) In 2017 the Company incurred gains as a result of a partial cancelation of a provision for the impairment of buildings in the United States that had been performed in the past.

Note 22 - Supplementary information to the statement of income items (cont.)

f. Financing revenues (expenses)

	For the year ended December 31		
	2017	2016	2015
	Dollars thousands		
Financing revenues			
Interest revenues from securities available for sale	-	-	2
Net gain from change in rates of exchange	-	-	469
Revaluation of liability for options to banks	75	9	-
	75	9	471
Financing expenses			
Financing expenses for short-term credit and bank loans	1,323	1,186	1,049
Net loss from change in foreign exchange rates	462	240	-
Reduction of discounting of options to banks	26	34	32
Net change in fair value of cash flow hedging transferred from shareholders' equity	-	-	505
Revaluation of liability for options to banks	-	-	83
Loss from realization of securities	-	-	171
Bank expenses and other expenses	1,081	1,204	888
	2,892	2,673	2,728

Note 23 - Earnings (loss) per share

Detail of number of shares and earnings (loss) used to calculate the earnings (loss) per share

	For the year ended December 31,					
	2017		2016		2015	
	Weighted average number of shares	Loss attributed to shareholders of the Company	Weighted average number of shares	Loss attributed to shareholders of the Company	Weighted average number of shares	Loss attributed to shareholders of the Company
	Thousands	Dollars thousands	Thousands	Dollars thousands	Thousands	Dollars thousands
For the purpose of calculating basic and diluted net loss	11,870	(3,199)	11,870	(1,121)	9,720	(3,938)

Note 24 – Operating segments

a. General

The information that the Company provides in accordance with the IFRS 8 definitions is based on the available financial information which is reviewed regularly and is used by the Company's CEO who is the Company's chief operating decision maker (CODM), for the purpose of making decisions regarding the resources to be allocated to the segment and in order to evaluate the segment's performance.

Based on the criteria in IFRS 8 for determining reportable operating segments, and the available financial information which is reviewed by the Company's CEO, the Company has determined that it operates in two reportable operating segments:

(a) Brands – This segment engages in the design, development, production and marketing of seamless intimate apparel and activewear and leisurewear, to customers in North America and Europe with leading brands such as Under Armour.

(b) Retail – This segment engages in the design, development, production and marketing of seamless intimate apparel and activewear and leisurewear which are characterized by purchasing large quantities of less complex products to private brands as well as brands for which the Company received a franchise to customers in the retail market in North America and Europe such as Wal-Mart.

b. Information on reportable segment sales, income (losses) and assets:

(a) Measurement of segment sales, income (losses) and assets:
Segment sales, income (losses) and assets are measured according to the same accounting principles as those applied in the consolidated financial statements.
The income (losses) of the segments reflect the profit (loss) from the operations of the segment and do not include net financial expenses and income taxes, since these items are not attributed to segments and are not analyzed by the CODM by segment.

(b) The segments' assets mostly include inventory, trade receivables and other receivables. Assets not attributed to the segments mostly include fixed assets, intangible assets, cash, financial derivative and deferred taxes.

c. Primary segment reporting in respect of business segments

	For the year ended December 31, 2017			
	Brands	Retail	Adjustments	Total
	Dollars thousand			
Total segment revenues	38,926	82,573		121,499
Direct profit (loss)	(8,642)	12,548		3,906
Indirect costs	(1,349)	(2,858)		(4,207)
Segment results	(9,991)	9,690		(301)
Financing expenses, net				(2,817)
Tax expenses				(81)
Loss				(3,199)
Segment assets	17,404	29,195	27,512	74,111
Segment liabilities	9,507	14,823	25,919	50,249
Cost of purchasing long-term assets	-	-	1,902	1,902
Depreciation and amortization	-	-	4,940	4,940

Note 24 – Operating segments (cont.)

c. Primary segment reporting in respect of business segments (cont.)

	For the year ended December 31, 2016			
	Brands	Retail	Adjustments	Total
	Dollars thousand			
Total segment revenues	40,302	76,100		116,402
Direct profit (loss)	(5,211)	11,767		6,556
Indirect costs	(1,485)	(2,746)		(4,231)
Segment results	(6,696)	9,021		2,325
Financing expenses, net				(2,664)
Tax expenses				(782)
Loss				(1,121)
Segment assets	22,695	22,360	30,501	75,556
Segment liabilities	12,185	8,259	27,917	48,361
Cost of purchasing long-term assets	-	-	1,675	1,675
Depreciation and amortization	-	-	5,156	5,156

	For the year ended December 31, 2015			
	Brands	Retail	Adjustments	Total
	Dollars thousand			
Total segment revenues	41,670	51,416		93,086
Direct profit (loss)	(1,669)	4,185		2,516
Indirect costs	(1,879)	(2,318)		(4,197)
Segment results	(3,548)	1,867		(1,681)
Financing expenses, net				(2,257)
Loss				(3,938)
Segment assets	16,294	21,876	33,822	71,992
Segment liabilities	8,492	6,985	28,184	43,661
Cost of purchasing long-term assets	-	-	4,844	4,844
Depreciation and amortization	-	-	4,898	4,898

Note 24 – Operating segments (cont.)

d. Secondary reporting regarding geographical segments

1. Sales by geographic markets (based on customer location):

	For the year ended December 31		
	2017	**2016**	**2015**
	Dollars thousands		
North America	111,206	114,083	88,495
Europe	10,201	753	3,623
Israel	92	1,566	968
	121,499	116,402	93,086

2. Carrying amount of assets and capital expenditures by geographical areas (based on asset location):

	Balance of non-current assets (*) December 31,		Capital expenditures for the year ended December 31		
	2017	**2016**	**2017**	**2016**	**2015**
	Dollars thousands				
Israel	20,750	23,738	1,481	1,474	4,704
North America	2,315	2,109	279	102	122
Others	294	81	142	99	18
	23,359	25,928	1,902	1,675	4,844

(*) Excluding deferred taxes, net.

e. Major customers

	For the year ended December 31		
	2017	**2016**	**2015**
	Percentage of total sales		
Customer A (part of the retail segment)	43.6	46.6	33.5
Customer B (part of the brands segment)	16.5	2.4	0.5
Customer C (part of the retail segment)	15.2	14.8	16.5
	75.3	63.8	50.5

Note 25 - Balances and transactions with interested parties and related parties

a. Balances with interested parties and related parties

Composition:

As at December 31, 2017

	Linkage terms	Related and interested parties	Key executives
		Dollars thousands	
Trade receivables		8.615	-
Trade payable	Unlinked	(696)	(34)
Subordinated loan from a shareholder		(1,852)	-
		6,067	(34)

As at December 31, 2016

	Linkage terms	Related and interested parties	Key executives
		Dollars thousands	
Trade receivables		5,742	-
Trade payable	Unlinked	(222)	-
Other payables		-	(121)
		5,521	(121)

b. Benefits to interested parties and related parties

	For the year ended December 31		
	2017	2016	2015
	Percentage of total sales		
Salaries and benefits for employees of the Company or on its behalf, including the CEO	321	304	362
Fees of directors not employed by or on behalf of the Company	247	230	302
Number of beneficiaries of salaries and benefits			
Related and interested parties employed by or on behalf of the Company	1	1	1
Directors not employed by the Company	5	8	11
	6	9	12

Note 25 - Balances and transactions with interested parties and related parties (cont.)

c. Transactions with related parties and interested parties

For the year ended December 31, 2017

	Related and interested parties	Executive officers
Sales	56,498	-
Cost of sales	(687)	-
Sales and marketing expenses	(114)	-
General and administrative expenses	(247)	(321)

For the year ended December 31, 2016

	Related and interested parties	Executive officers
Sales	56,561	-
Cost of sales	(441)	-
Sales and marketing expenses	(23)	-
General and administrative expenses	(230)	(304)

For the year ended December 31, 2015

	Related and interested parties	Executive officers
Sales	34,948	-
Cost of sales	(87)	-
Sales and marketing expenses	(824)	-
General and administrative expenses	(308)	(362)

d. An investment agreement with Litef Holdings Inc.

On February 17, 2015, the Company signed with its controlling shareholder, Litef Holdings Inc., a private company incorporated in Canada (hereinafter: "Litef"), an agreement pursuant to which Litef shall invest a total of US 5 million dollars against an extraordinary private placement of 4,672,897 ordinary shares of the Company of NIS 10 par value each (hereinafter: "ordinary shares"), so that Litef shall pay a price of US 1.07 dollars per share.

On May 25, 2015, a special meeting of the shareholders of the Company was convened during which the private placement was approved and on May 31, 2015, the private placement was completed, in accordance with its terms. For additional details see Note 20a above.

e. Agreement for a real estate property lease in the U.S. with an interested party

On September 7, 2014, the Company's shareholders' meeting approved, upon receiving the approval of the Company's Audit Committee and Board of Directors, the engagement of the company Tefron USA, Inc., a wholly-owned private company, indirectly, of the Company (hereinafter: "Tefron USA"), with Trimfit Global Inc., a private company

Note 25 - Balances and transactions with interested parties and related parties (cont.)

e. Agreement for a real estate property lease in the U.S. with an interested party (cont.)

incorporated in Delaware, USA, related to the Nouvelle Group who is amongst the controlling shareholders of the Company (hereinafter: "Trimfit") in an agreement for a real estate property lease which is owned by Tefron USA in Valdese, North Carolina, USA, in an area of about 170,000 square feet, which is used as a center for logistics, for a consideration of US 108 thousand dollars per year, for a period of two years as of September 1, 2014 with an option of extension for an additional year. Furthermore, it was agreed upon between the parties in the framework of the aforementioned engagement, that Trimfit would provide Tefron USA, according to its needs, sorting, picking and delivering services (Pick and Pack) (hereinafter: “the services”), for a consideration that is equal to the cost of receiving these services through a subcontractor (hereinafter: “the agreement”).

In the framework of the agreement with Trimfit, the consideration of the lease fees, was determined by negotiation between the Company and Trimfit, and based on an expert assessment, conducted by an external and independent appraiser office in North Carolina (Integral Realty Resources-Greensboro), which was based, amongst other things, on the comparison data of the lease fees and similar leased property that is in the vicinity of the property. In accordance with the aforementioned assessment, the appropriate annual lease fee for the property is in the price range between US 0.62 dollars per square feet to US 0.72 dollars per square feet. The lease fees stipulated in the agreement is based on an annual consideration of approximately US 0.64 dollars per square feet.

Tefron USA would be entitled to receive these services from Trimfit. The consideration agreed upon between the parties in respect of granting the services by Trimfit to the Company, as the Company shall require these services, shall be determined by an annual comparison to the prices of a subcontractor who provides similar services to the Company and is not related to the Company and/or to any of its controlling shareholders. The aforementioned agreement expired on August 31, 2016.

f. Lease agreement with a related party

On March 28, 2016, the Company's Board decided, after obtaining the approval of the Audit Committee of the Company, to approve the engagement of the Company in a non-extraordinary transaction, as this term is defined in the Companies Law, with a subsidiary of Lamour, for the purpose of sublease of office space in Montreal, Canada, in an area of 540 square meters for a monthly payment of US 3,950 dollars (excluding taxes). The approval of the Company’s Board, as stated above, will remain in effect for a period of up to three years.

g. Agreement for invoicing services with a related party

In February 2012, the Company's Board approved, following the approval of the Audit Committee of the Company, the Company's engagement in a non-extraordinary transaction with Lamour which shall serve as a channel for the sale of the Company’s products to Wal-Mart, and this for the reasons described below: Wal-Mart is a significant customer of the Company. In order for the Company to sell products directly to Wal-Mart, it must first complete the process of issuing a manufacturer’s identification number. As of this date, the Company has not yet completed the process of issuing the said manufacturer’s identification number due to the difficulty to obtain it opposite Wal-Mart. In light of the aforesaid, the Company decided to sell its products to Wal-Mart through Lamour which already acquires a Wal-Mart’s manufacturer’s identification number. According to the agreements between Lamour and the Company, the proceeds from Wal-Mart which is paid to Lamour, is transferred to the Company upon receiving it and under the same payment

Note 25 - Balances and transactions with interested parties and related parties (cont.)

g. Agreement for invoicing services with a related party (cont.)

terms. On March 22, 2015, and March 29, 2018, the Company's Board approved the extension of the term of the agreement for additional 3 years, after receiving the recommendation of the Audit Committee according to which the extension of the period, as aforementioned, is reasonable under the circumstances.

h. Lease agreement with a related party

On December 30, 2013, the Company's Board of directors approved, following the approval of the Company's Audit Committee, the Company's engagement in a non-extraordinary transaction, as this term is defined in the Companies Law, with Asia Socks for the purpose of subleasing office space in Shanghai China, on a total area of approximately 140 square meters for a daily payment of US 63 dollars (a total of US 1,890 dollars monthly), and this as of February 1, 2014. Moreover, upon the increase in the volume of activity of the representative of the Company in China, the lease agreement has been extended by an area of 395 square meters for a consideration of US 180 dollars per day (a total of US 5,400 dollars per month). On April 1, 2016 this agreement expired.

i. Service agreement for export license number with a related party

On December 17, 2014, the Company's Board approved, following the approval of the Company's Audit Committee, the engagement of the Company in a transaction which does not require the approval of the general meeting of the Company, pursuant to Regulation 1(2) of the Companies Regulations (Relief in Transactions with Interested Parties) 2000, between the Company and Asia Socks, according to which the Company will use, free of charge, the export license of Asia Socks for the purpose of importing raw materials, from various suppliers of raw materials, from China to Israel. It should be noted that the engagement with the raw material suppliers in China and the terms of engagement with them will be carried out by a representative of the Company and at the sole discretion of the Company, while the export process will be carried out by Asia Socks, without any consideration paid to Asia Socks for this service (the export will be on back to back terms to the terms of the procurement of raw materials). The transaction was approved for a period of three years and/or until the Company's subsidiary, who the Company intends to establish, acquires its own export license, when it shall be established. On December 2, 2016 the Company's subsidiary was established in China and this engagement is no longer required.

j. Payment of director remuneration to a related party

Pursuant to the resolution of the general meeting of the shareholders of the Company dated December 29, 2010, regarding the approval of granting remuneration to Mr. Guy Shamir (son of Mr. Meir Shamir who is among the controlling shareholders of the Company) (hereinafter: "Mr. Shamir"), in respect of his service as a director of the Company and since 3 years have passed as of the date of the approval, as aforesaid, on November 21, 2013, pursuant to the decision of the Remuneration Committee of the Company dated July 14, 2013, the Company's Board approved, in accordance with section 275(a1)(1) of the Companies Law, and in accordance with the provisions of Regulation 1b of the Companies Regulations (Relief in Transactions with Interested Parties) 2000, granting remuneration to Mr. Shamir in respect of his service as a director of the Company, in accordance with the director remuneration paid for the other directors of the Company, during 2015 the Company paid Mr. Guy Shamir US 8 thousand dollars (in 2014 – US 16 thousand dollars) for his service as a director of the Company. On June 1, 2015, Guy Shamir announced his resignation from the Board of the Company as of that date.

Note 25 - Balances and transactions with interested parties and related parties (cont.)

k. Payment of director remuneration to controlling shareholders

Pursuant to the appointment of Messrs. Ben Lieberman and Martin Lieberman (hereinafter: “Messrs. Lieberman”), who are amongst the controlling shareholders of the Company, as directors of the Company starting on August 12, 2015, on November 30, 2015, the Company’s Board approved, after obtaining the approval of the Company’s Remuneration Committee, the granting of director remuneration in accordance with the provisions of the Companies Regulations (Relief in Transactions with Interested Parties) 2000, as of the date of the commencement of their term of service as directors of the Company, in accordance with the director remuneration paid for the other directors of the Company. As of the date of Mr. Ben Lieberman's appointment as the CEO of the Company, he does not receive director remuneration.

l. Inclusion of a related party in the director and officer policy of the Company

Pursuant to the appointment of Messrs. Lieberman, who are amongst the controlling shareholders of the Company, as directors of the Company as of August 12, 2015, on November 30, 2015, the Company's Board approved, after obtaining the approval of the Remuneration Committee of the Company the inclusion thereof in the director and officer policy of the Company in accordance with the provisions of the Companies Regulations (Relief in Transactions with Interested Parties) 2000.

m. Granting a letter of indemnity to controlling shareholders

On February 11, 2016, the general meeting of the shareholders of the Company approved, after obtaining the approval of the Remuneration Committee and the Board of Directors of the Company, the granting of letters of indemnity to Messrs. Lieberman in the Company’s customary text and form for its officers.

n. Negligible transactions

On March 22, 2015, the Company adopted, after obtaining the approval of the Audit Committee and the Board of the Company, the procedure concerning transactions with interested parties and officers, in the framework of which the Company adopted guidelines and rules for the classification of a Company's transaction with an interested party as negligible.

As part of the procedure, it was determined that in any transaction that is tested for negligibility, all of the criteria relevant to such transaction will be examined prior to the event, such as the ratio of assets, ratio of liabilities, ratio of shareholders’ equity, ratio of revenues and the ratio of expenses, and in the event that the rate of each of the relevant standards is less than half a percent (0.5%) or less than 300,000 dollars, whichever is lower, the transaction shall be deemed as negligible, subject to the following:

1. In cases where, at the discretion of the Company, the aforementioned criteria are not relevant to the transaction at issue, the Company will determine another criterion provided that the relevant criterion concerning such transaction is at a rate of less than half a percent (0.5%) or less than 300,000 dollars, whichever is lower.

2. The negligibility of the transaction will be reviewed on an annual basis for the periodic report, the financial statements and prospectus (including shelf prospectus reports), while including all the transactions of the same type that have been carried out with an interested party or controlling shareholder, as applicable, in the same year.

3. A preliminary condition for the examination of a transaction whether it is negligible or not, is that the transaction is carried out under market conditions. Any transaction which is not being carried out under market conditions, does not meet the definition of a negligible transaction, and is considered as an extraordinary transaction which

Note 25 - Balances and transactions with interested parties and related parties (cont.)

n. Negligible transactions (cont.)

requires approval procedures as required by law in relation to an extraordinary transaction.

4. A transaction shall not be considered as negligible when it is not negligible from a qualitative standpoint. (Examination of the qualitative considerations of the transaction of the interested party may contradict the negligibility of the transaction, as noted above. For instance, and for the purpose of example only, a transaction with an interested party will not generally be considered as negligible if it is seen as a significant event by the Company's management and it serves as a basis for managerial decisions, or if in the framework of the transaction of the interested party, interested parties are expected to receive benefits and it is important to report them to the public).

o. Loans from the shareholders in an aggregate amount of US 2 million dollars

On September 27, 2017, the Company's Audit Committee and Board of Directors approved at their meetings a transaction to obtain a subordinated loan from a controlling shareholder of the Company, Litef Holdings Inc., a private Canadian company wholly owned and controlled by Ben Lieberman and Martin Lieberman. On September 28, 2017, the Company was granted a loan in the amount of US 1 million dollars (hereinafter: "the loan principal"), according to the following terms:

1. The principal of the loan shall bear annual interest at a rate equal to the annual interest of the US Government's annual bonds, on the basis of which the interest was set at 1.3% per annum (hereinafter: "the interest"). The interest and the loan principal shall be referred together as: "the loan".

2. The loan is not secured by any collateral.

3. The loan will be repaid by the Company until September 30, 2018 (hereinafter: "the maturity date"), subject to the provisions of Clause 4 as follows.

4. The loan is subordinated to the loans that the Company took from its financing banks - Bank Leumi Le-Israel Ltd., Bank Hapoalim Ltd. and Israel Discount Bank Ltd. (hereinafter: "the banks"), whereas according to its subordination terms, it could be repaid (in whole or in part, as applicable) only in the event where on the repayment date (a) the Company's tangible shareholders' equity will not be less than US 27.5 million dollars after the repayment of the loan (in whole or in part, as applicable), and (b) the Company will meet all of its obligations to the banks, including its undertaking to comply with financial covenants; all according to the reviewed quarterly financial statements of the Company as at June 30, 2018 (hereinafter together: "the preconditions for repayment of the loan").

5. If the preconditions for repayment of the loan are not fulfilled by the maturity date, in whole or in part, the fulfillment of the preconditions will be reexamined at the subsequent date of approval of the Company's financial statements, audited or reviewed, as applicable, and so forth (hereinafter: the "periodic examination date"), and if at the time of the periodic examination date the preconditions for repayment of the loan are fulfilled, the loan will be repaid, in whole or in part, as applicable, within 30 days as of the periodic examination date.

6. The Company is given the possibility of an early repayment of the loan, in whole or in part, at its sole discretion, without requiring any other additional consideration in

Note 25 - Balances and transactions with interested parties and related parties (cont.)

o. Loans from the shareholders in an aggregate amount of US 2 million dollars (cont.)

respect of the loan in regards with the early repayment, provided that it complies with the covenants stated in Clause 4 above.

On December 28, 2017, the Company received an additional loan of US 1 million dollars from the controlling shareholders. The additional loan was granted under similar conditions to the first loan (1.7% interest).

As at the date of this report the repayment date of the two loans is January 1, 2019.

p. Approval of the remuneration policy for officers of the Company

On March 27, 2017, the General Meeting of the Company approved the updated remuneration policy for officers of the Company. On August 3, 2017, the General Meeting of the Company approved to amend the annual bonus clause in the remuneration policy for officers of the Company, subject to the recommendations of the Remuneration Committee at its meeting dated June 18, 2017.

t. The Company’s engagement with Mr. Ben Lieberman in an agreement to provide management services to the Company as CEO

On February 1, 2017, Mr. Ben Lieberman, a director and controlling shareholder of the Company, was appointed as Acting CEO until the appointment of a new CEO for the Company. On May 4, 2017, the General Meeting of the shareholders of the Company approved the engagement of the Company with Mr. Ben Lieberman in an agreement to provide management services to the Company as Acting CEO. On June 18, 2017, the Company’s Board decided to appoint Mr. Lieberman as the Company’s CEO as of June 19, 2017. On August 3, 2017, the Company’s General Meeting approved the engagement with Mr. Lieberman in an agreement to provide management services to the Company as CEO.

u. Approval of a transaction between the Company and its controlling shareholders for the purpose of leasing showrooms

On August 24, 2017, the Company's Audit Committee and Board of Directors approved a transaction between the Company and its controlling shareholders. The transaction revolves around three companies jointly renting showrooms in Manhattan, New York, which will be used by the three companies (1/3 each) for the purpose of presenting their products. For this purpose, the Company (through a wholly-owned subsidiary) will engage in an agreement with a private company controlled by the controlling shareholders of the Company, Ben Lieberman and Martin Lieberman (hereinafter: "the lessee"), whereby the lessee will lease to the Company, through a back-to-back lease, part of the showrooms’ space which the lessee leased in a building in Manhattan, New York, which constitute one-third of the showrooms, which will serve, as aforementioned, the three companies (hereinafter: the "showroom complex"). The three companies are the Company and two other companies, one of which is owned by the said controlling shareholders, and the other is a company in which the controlling shareholders own 50%. All three companies operate in the textile sector, while the Company is the only company operating in the field of seamless technology. The holding of a joint showroom complex by a number of companies is acceptable, when it serves all of the companies participating in it, which enjoy greater exposure and exploit economies of scale (hereinafter: "the lease agreement").

The terms of the engagement are as follows:

a. As aforesaid, the terms of the lease agreement will be back-to-back to the terms of the lease agreement signed between the lessee and the owners of the showroom complex

Note 25 - Balances and transactions with interested parties and related parties (cont.)

u. Approval of a transaction between the Company and its controlling shareholders for the purpose of leasing showrooms (cont.)

(hereinafter: the "main lease agreement"), when it refers to 1/3 of the showroom complex area. The lease refers to 290 square meter (gross) (3,147 square feet) of the showroom complex area which constitutes one-third of the area of the entire showroom complex. The two additional companies will each bear a third of the lease fees of the showroom complex.

b. The lease term - the lease term is as of July 1, 2017 and until December 31, 2021.

c. The lease fees - for the sublease, the Company will pay a 1/3 of the lease costs of the showroom complex, on the dates of their payment, as stipulated in the main lease agreement. Accordingly, the cost of the lease fees for the Company will be 11,500 dollars monthly.

d. Other joint expenses - In addition to the lease fees, the Company will bear one-third of the additional current expenses of the showroom complex, such as cleaning expenses, maintenance costs, water, electricity, municipal taxes, etc. The cost of the joint expenses for the Company is estimated at 1,150 dollars per month.

e. Showroom complex renovation expenses - The renovation and adjustment work was carried out by a third party unrelated to any of the three companies, whereas each of the companies bears a third of the renovation and adjustment costs. The Company's share in this renovation is US 154,000 dollars.

v. The Company' merger with a wholly-owned subsidiary

On December 21, 2016, the Boards of Directors of the Company (hereinafter: "the acquiring company") and of the wholly owned subsidiary of the Company Hi-Tex founded by Tefron Ltd. ("the target company"), approved the merger between the companies so that on the date of the merger the target company will merge with and into the receiving company, so that the target company ceases to exist as a separate legal entity and will be dissolved without liquidation, while the acquiring company will own all assets, rights, agreements, authorities and powers and will be charged with any debt and/or undertaking of the target company. The agreement regarding the merger was signed by the companies on December 22 and on September 29, 2017 and October 30, 2017 an additional amendment to the agreement was signed, extending its validity for an additional period the last of which is December 31, 2017. Accordingly, to the extent that the conditions precedent specified in the agreement are not fulfilled for any reason until December 31, 2017, and the parties have not agreed to extend this date, then either party may cancel this agreement, and the other party shall have no claim and/or demand against the other party in connection therewith.

On December 26, 2017, a decision was made regarding the taxation of the agreement concerning the merger of Hi-Tex, founded by Tefron Ltd. with and into Tefron Ltd., in accordance with the provisions of Section 103b of the Ordinance.
The date of the merger was set for December 31, 2016, and all as determined and detailed in the merger decision and subject to the terms of Section E2 of the Ordinance, including:

a. No new rights will be allocated to the shareholders of the acquiring company due to the merger.

b. The provisions of Section 103e of the Ordinance and provisions of Section 103c(2) shall apply to the assets transferred to the acquiring company.

c. Section 103h will be implemented, so that the losses of the companies participating in the merger that are transferable will be allowed to be offset against the income of the acquiring company starting from the tax year following the merger, provided that in any tax year this amount is no more than 20% (five-year spread) of the total losses of

Note 25 - Balances and transactions with interested parties and related parties (cont.)

v. The Company' merger with a wholly-owned subsidiary (cont.)

the transferring company and the acquiring company or 50% of the taxable income of the acquiring company in that tax year before offsetting the loss from previous years, whichever is lower.

d. Advances in respect of excess on the eve of the merger will be offset as determined in the taxation decision.

e. A succession of rights will apply in respect of the transferred employees.

On February 18 the merger was completed.

Note 26 - Events subsequent to the balance sheet date

On March 22, 2018, the Company received the consent of the banks which finance the Company's operations, Bank Leumi Le-Israel Ltd., Israel Discount Bank Ltd. And Bank Hapoalim Ltd. (hereinafter: the "banks") according to which for the purpose of replacing the financing of the Company's operations in financing led by a foreign bank and/or banks (if and to the extent that such financing is received), the banks agree that the Company will repay its debts to the banks in an early repayment in such a manner that 82% of the debts will be repaid and the remaining 18% will be forgiven by the banks (hereinafter: the "early repayment").
A condition for the early repayment is a change in the exercise price of 300,000 options allocated by the Company to the banks, so the exercise price shall be US 1 dollar instead of US 1.43.

a. The aforesaid consent is subject to the early repayment being made no later than April 26, 2018. If such repayment as aforesaid is not carried out, the existing debt arrangement between the Company and the banks will remain in effect. The total debt of the Company to the banks as at March 20, 2018 amounted to US 23.6 million dollars. The early repayment, if carried out, will include a payment to the banks of an estimated early repayment fee of approximately US 160,000 dollar.

b. On March 29, 2018, a financing agreement was signed with the following parties: Tefron Canada Inc., a private Canadian subsidiary wholly-owned by the Company, as the borrower (hereinafter: "Tefron Canada"), the Company, as the parent company (hereinafter: "Tefron Israel") and the bank HSBC Canada (hereinafter: "the bank"), for the purpose of providing alternative financing to the current bank financing (hereinafter: the "agreement") whose principal terms are as follows:

1. The financing that will be provided will amount to a total cumulative fund of up to $ 38,000,000 (US dollars) which will be divided as follows:

(1) Credit to Tefron Canada in the amount of $ 13,000,000 by means of a bank guarantee that shall guarantee providing credit to Tefron Israel through HSBC Israel (hereinafter: the "**bank in Israel**"), as follows: (a) a long-term loan in the principal amount of $ 10,000,000 (hereinafter: the "**long-term loan**"), and (b) credit for working capital in the principal amount of $ 3,000,000. It should be noted that any repayment of the long-term loan, in whole or in part, as applicable, will reduce the amount of the aforesaid credit line in the sum of $ 13,000,000, respectively;

(2) Credit up to an amount of $ 25,000,000 that shall be provided to Tefron Canada by the bank on the basis of volume of collateral, which will be examined monthly. The eligibility for credit withdrawals will be based on the following eligibility amounts:

a. Cumulative debt amounts of the trade receivables of Tefron Canada and the trade receivables of Tefron Israel's subsidiary, Tefron USA Inc. (hereinafter: "**Tefron USA**"), all in accordance with the terms of the agreement (with a multiplier of 75% - 90% according to the type of customer); plus;

Note 26 - Events subsequent to the balance sheet date (cont.)

b. (cont.)

b. The lower of: (1) 50% of the inventory value of the finished goods of Tefron Canada and Tefron USA, subject to pledges under the agreement; and (2) $ 10,000,000; plus;

c. 100% of the value of the cash in the bank accounts of Tefron Canada and Tefron USA; plus;

d. 50% of the appraised value of 2 real estate properties owned by Tefron USA in North Carolina, USA, after these properties are pledged in accordance with the provisions of the agreement;

Less amounts secured by a pledge which has priority or may have priority over the collateral given to the bank pursuant to the agreement.

As at the date of this report (assuming that the Company's existing financing is replaced by the new financing provided by the bank), in accordance with the above terms, Tefron Canada has credit eligibility of approximately $ 12,000,000, which together with the financing described in sub-clause (1) above, will reach a total immediate funding of $ 25,000,000.

2. In addition to the financing mentioned in Clause 1 above, the bank will provide, at its discretion, a facility for the execution of hedging transactions on interest differentials in the amount of $ 4,000,000 and a facility for the execution of hedging transactions on currency exchange differences in the amount of $ 2,300,000.

3. The long-term loan will be repaid in seven equal annual payments, and in any event where there is free cash flow, the repayment will be accelerated (within 120 days as of the end of the calendar year) at a rate of one percent of the free cash flow determined by Tefron Israel's annual EBITDA (on consolidated basis), based on the ratio of debt to EBITDA[1] of Tefron Israel, on a consolidated basis, as follows:

When R represents the ratio of debt to EBITDA:	Percentage of repayment of the free cash flow
$R \leq 1.00$	0%
$1.00 < R \leq 2.00$	15%
$2.00 < R \leq 3.00$	25%
$R > 3.00$	40%

When for this purpose the "free cash flow" is the amount of EBITDA less interest payments, tax payments, unfinanced investments and principal payments of the long-term loan according to its amortization schedule.

4. The interest on the financing will be variable interest, which will include a margin above the base interest rate, such as LIBOR or prime as detailed as follows:

When R represents the ratio of debt to EBITDA:	Percentage of margin
$R \leq 1.50$	2.25% - 1.25%
$1.50 < R \leq 2.00$	2.5% - 1.5%
$2.00 < R \leq 3.00$	2.75% - 1.75%
$R > 3.00$	3% - 2%

[1] In the framework of the agreement, it was agreed upon that in respect of the period of up to September 30, 2018, to the calculation of EBITDA according to the financial statements and in accordance with the terms of the agreement, will be added an amount of US 2 million dollars.

Note 26 - Events subsequent to the balance sheet date (cont.)

b. (cont.)

5. The collateral for the financing will be as follows:
   a. First ranking charge in Canada by Tefron Canada on all of its assets.
   b. Floating and fixed charge first in rank in Israel on all assets of Tefron Israel.
   c. First ranking charge on all shares held by Tefron Israel in Tefron Canada Inc. and Tefron US Holdings Inc. (a subsidiary holding Tefron USA).
   d. First ranking charge on the bank accounts of Tefron Israel and its subsidiaries.
   e. Tefron Israel and its subsidiaries' guarantee to the debts of Tefron Canada to the bank.
   f. The guarantee of EDC - Export Development Canada, which assists the Canadian government in financing the export activities of Canadian companies, in an amount equal to 75% of the credit limit on the sum of $ 13,000,000 given to the bank in Israel by the bank.

6. The financing is subject to the fulfillment of the financial covenants which will be examined on a quarterly basis on the basis of the financial statements of Tefron Israel, on a consolidated basis, as follows:
   a. Debt service cover ratio of at least 1.25 times.
   "Debt service cover ratio" means - for the last consecutive twelve months preceding the calculation date, the ratio between the total payments to the bank (principal and interest) and net EBITDA (as defined in the agreement).
   b. Debt to EBITDA ratio of no more than:
      (1) 6.00X for the quarter ending March 31, 2018.
      (2) 4.00X for the quarter ending June 30, 2018.
      (3) 3.50X at any time thereafter.

7. In accordance with the agreement, Tefron Israel and its subsidiaries in connection with the financing are subject, *inter alia*, to the following restrictions:
   a. A negative pledge by Tefron Israel and its subsidiaries (excluding pledges permitted under the agreement);
   b. Until full repayment of the provided credit, Tefron Israel will continue to hold, directly or indirectly, full ownership of each of its subsidiaries;
   c. The Lieberman family will continue to hold the control of the Company;
   d. The total amount of annual investments of the Group shall not exceed $ 2,000,000;
   e. Prohibition on taking loans as defined in the agreement;
   f. Prohibition of dividend distribution.

8. The agreement determines that the financing is at the bank's full discretion at any time, and in addition, in the framework of the agreement accepted grounds for immediate repayment were determined, granting the bank the right to call for an immediate repayment of Tefron Canada's liabilities to it, including upon the occurrence of a breach of Tefron Israel's loan agreements with HSBC Israel and/or a breach by any party of Tefron Group of the agreements or other documents relating to the provision of the credit and/or in an amount exceeding $ 750,000.

   The financing according to the agreement will enable the Company to carry out the early repayment to its financing banks in accordance with the terms detailed in Note 26a above. The provision of the financing and the execution of the early repayment are expected to take place in the second week of April 2018.

Details regarding significant subsidiaries held by the Company as at December 31, 2017:

Name of the subsidiary	Country of incorporation and principal place of business activity	% of rights of ownership as at December 31, 2017 %	2016 %
Tefron - Macro Ltd	Israel	100%	100%
Tefron USA Inc., wholly-owned by Tefron US Holdings, Corp	U.S.A	100%	100%
El-Masira Textile Co., wholly-owned by Tefron USA Inc.	Jordan	100%	100%
Tefron Canada Inc.	Canada	100%	100%
Tefron Hong Kong Limited	Hong Kong	100%	100%
Tefron Holdings (98) Ltd.	Israel	100%	100%
Tefron Trading (Shanghai) Company Limited – owned by Tefron Hong Kong	China	100%	100%