

TEFRON LTD

INTERIM CONSOLIDATED FINANCIAL STATEMENTS

AS AT SEPTEMBER 30, 2011

UNAUDITED

CONTENTS

	<u>Page</u>
Review of the interim consolidated financial statements	1
Consolidated balance sheet	2-3
Consolidated statements of income	4
Consolidated statement of comprehensive income	5
Consolidated statements of changes in shareholders' equity	6-7
Consolidated statements of cash flows	8-9
Notes to the interim consolidation financial instruments	10-19

ERNST & YOUNG
Kost Forer Gabbay & Kasierer

Review Report of the Auditors to the Shareholders of Tefron Ltd.

Preface

We have reviewed the attached financial information of Tefron Ltd. and its subsidiaries (hereinafter – the Group) which includes the condensed consolidated balance sheet as at September 30, 2011 and the condensed consolidated statements of income, comprehensive income, changes in shareholders equity and cash flows for the periods of six months and three months then ended. The Board of Directors and Management are responsible for the preparation and presentation of the financial information for these interim periods in accordance with International Accounting Standard IAS 34 – “Financial Reporting for Interim Periods”, and they are responsible and they are responsible for the preparation of financial information for these interim periods under Chapter D’ of the Securities Regulations (Periodic and Immediate Reports) – 1970. Our responsibility is to express a conclusion on the financial information for these interim periods, based on our review.

Scope of the review

We performed our review in accordance with Review Standard 1 of the Institute of Certified Public Accountants in Israel “Review of Financial Information for Interim Periods Prepared by the Entity’s Auditor”. A review of financial information for interim periods comprises clarifications, mainly with the people responsible for financial and accounting matters, and applying other analytical review procedures. A review is considerably more limited in scope than an audit carried out in accordance with generally accepted auditing standards in Israel, and therefore does not enable us to achieve with sufficient certainty that we will be aware of all significant matters which could have been identified in an audit. Consequently we are not expressing an opinion of an audit.

Conclusion

Based on our review, we are not aware of any fact which would cause us to think that the above financial information has not been prepared, in all significant aspects, in accordance with International Accounting Standard IAS 34.

In addition to the aforesaid in the previous paragraph, based on our review, we are not aware of anything which could cause us to think that the above financial information does not meet, from all significant aspects, the disclosure provisions under Chapter D of the Securities Regulations (Periodic and Immediate Reports) – 1970.

Without qualifying our above conclusions, we direct attention to Note 1c of the financial statements, regarding the Company’s business and losses, the uncertainty connected with meeting the financial covenants with the banks and regarding Management’s plans.

Haifa,
November 22, 2011

Kost, Forer, Gabbay & Kasierer
Certified Public Accountants

Consolidated balance sheets

	As at September 30,		As at December 31,
	2011	2010	2010
	Unaudited		Audited
Dollars thousands			
<u>Current assets</u>			
Cash	5,652	1,948	9,361
Investment in securities available for sale	686	700	731
Trade receivables	13,671	9,430	9,339
Other receivables	2,072	2,080	1,878
Inventory	17,475	15,625	16,664
	39,556	29,783	37,973
<u>Non current assets held for sale</u>			
	5,226	176	2,088
	44,782	29,959	40,061
<u>Non current assets</u>			
Deferred taxes, net	1,149	1,488	972
Property, plant and equipment, net	32,072	50,997	38,936
Software	191	243*	280*
Goodwill, backlog and other intangible assets	1,778	417*	2,503*
	35,190	53,145	42,691
	\$ 79,972	\$ 83,104	\$ 82,752

* Reclassified

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

TEFRON LTD

Consolidated balance sheets

	As at September 30,		As at December 31,
	2011	2010	2010
	Unaudited		Audited
	Dollars thousands		
<u>Current liabilities</u>			
Credit from banks	\$ 7,197	\$ 25,260	\$ 6,194
Trade payables	13,615	8,981	11,864
Other payables	4,695	3,454	8,450
	25,507	37,695	26,508
<u>Non current liabilities</u>			
Long-term bank loans	22,094	-	19,818
Employees benefits, net	445	486	516
Long-term institutions payable	-	1,473	-
Deferred taxes, net	-	635	-
	22,539	2,594	20,334
<u>Equity attributable to the equity holders of the Company</u>			
Share capital	19,818	10,351	19,818
Additional paid-in capital	107,948	108,942	107,204
Accumulated deficit	(88,486)	(69,138)	(83,803)
Treasury shares	(7,408)	(7,408)	(7,408)
Capital reserve for financial assets available for sale	(57)	(122)	(91)
Capital reserve for hedging transactions	(79)	-	-
Capital reserve for transactions with a controlling shareholder	190	190	190
	31,926	42,815	35,910
<u>Total capital</u>	31,926	42,815	35,910
	\$ 79,972	\$ 83,104	\$ 82,752

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

November 22, 2011
Date of approval of the
financial statements

Arnon Tieberg
Chairman of the Board

Amit Meridor
CEO

Eran Rotem
CFO

TEFRON LTD

Consolidated statements of income

	For the nine months ended		For the three months ended		Year ended
	September 30,		September 30,		December 31
	2011	2010	2011	2010	2010
	Unaudited				Audited
In dollars thousands					
Sales	\$ 86,885	\$ 68,709	\$ 30,119	\$ 17,990	\$ 86,044
Cost of sales, net*	73,088	63,981*	25,541	17,341*	83,990*
Gross profit	13,797	4,728	4,578	649	2,054
Development expenses, net (*)	2,782	1,946*	731	427*	2,869*
Selling and marketing expenses	12,154	9,123	3,636	2,527	11,850
General and administrative expenses	2,583	2,440	756	642	4,050
Other expenses	-	133	-	133	6,091
Operating loss	(3,722)	(8,914)	(545)	(3,080)	(20,806)
Financial income	498	271	484	7	30
Financial expenses	(1,523)	(2,048)	(557)	(876)	(2,379)
Financial expenses, net	(1,025)	(1,777)	(73)	(869)	(2,349)
Loss before taxes on income	(4,747)	(10,691)	(618)	(3,949)	(25,155)
Tax benefit	189	2,365	89	872	2,469
Loss	\$ (4,558)	\$ (8,326)	\$ (529)	\$ (3,077)	\$ (22,686)
<u>Loss per share attribute to the Company's shareholders (in dollars)</u>					
Basic and diluted loss per share	<u>\$ (0.7)</u>	<u>\$ (2.9)</u>	<u>\$ (0.1)</u>	<u>\$ (1.0)</u>	<u>\$ (7.7)</u>
EBITDA	<u>\$ 1,658</u>	<u>\$ (1,743)</u>	<u>\$ 883</u>	<u>\$ (589)</u>	<u>\$ (6,630)</u>

* Reclassified

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

Consolidated statements of comprehensive income

	For the nine months ended		For the three months ended		Year ended December 31 2010
	September 30,		September 30,		
	2011	2010	2011	2010	2010
	Unaudited				Audited
	In dollars thousands				
Loss	<u>\$ (4,558)</u>	<u>\$ (8,326)</u>	<u>\$ (529)</u>	<u>\$ (3,077)</u>	<u>\$ (22,686)</u>
Other comprehensive (loss):					
Gain realized on cash flow hedges	(184)	(115)	(80)	-	(115)
Unrealized gain (loss) from cash flow hedges	105	-	(79)	-	-
Unrealized gain (loss) on securities investments available for sale	34	(36)	12	-	(5)
Actuarial loss on defined benefit programs	<u>(125)</u>	<u>(146)</u>	<u>-</u>	<u>(146)</u>	<u>(451)</u>
Total other comprehensive loss	<u>(170)</u>	<u>(297)</u>	<u>(147)</u>	<u>(146)</u>	<u>(571)</u>
Total comprehensive loss attribute to the Company' shareholders	<u>\$ (4,728)</u>	<u>\$ (8,623)</u>	<u>\$ (676)</u>	<u>\$ (3,223)</u>	<u>\$ (23,257)</u>

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

Consolidated statements of changes in equity

	Relating to the Company's shareholders							Total equity
	Share capital	Additional paid-in capital	Retained deficit	Treasury shares	Capital reserve for available for sale financial assets	Capital reserve for cash flow hedges	Capital reserve with a controlling shareholder	
	Unaudited							
	Dollars thousands							
<u>Balance as at January 1, 2011</u> <u>(audited)</u>	\$ 19,818	\$ 107,204	\$ (83,803)	\$ (7,408)	\$ (91)	\$ -	\$ 190	\$ 35,910
Total comprehensive income (loss)	-	-	(4,683)	-	34	(79)	-	(4,728)
Share-based payment	-	744	-	-	-	-	-	744
<u>Balance As at September 30,</u> <u>2011 (Unaudited)</u>	<u>19,818</u>	<u>107,948</u>	<u>(88,486)</u>	<u>(7,408)</u>	<u>(57)</u>	<u>(79)</u>	<u>190</u>	<u>31,926</u>
<u>Balance as at January 1, 2010</u> <u>(audited)</u>	\$ 7,518	\$ 107,522	\$ (60,666)	\$ (7,408)	\$ (86)	\$ 115	\$ -	\$ 46,995
Total comprehensive loss	-	-	(8,472)	-	(36)	(115)	-	(8,623)
Share-based payment	-	440	-	-	-	-	-	440
Rights offering (less issue expenses net of \$187 thousand)	2,833	980	-	-	-	-	-	3,813
Capital benefit from a transaction with a controlling shareholder	-	-	-	-	-	-	190	190
<u>Balance As at September 30,</u> <u>2010 (Unaudited)</u>	<u>10,351</u>	<u>108,942</u>	<u>(69,138)</u>	<u>(7,408)</u>	<u>(122)</u>	<u>-</u>	<u>190</u>	<u>42,815</u>
<u>Balance as at July 1, 2011</u>	19,818	107,427	(87,957)	(7,408)	(69)	80	190	32,081
Total comprehensive income (loss)	-	-	(529)	-	12	(159)	-	(676)
Share-based payment	-	521	-	-	-	-	-	521
<u>Balance As at September 30,</u> <u>2011 (Unaudited)</u>	<u>19,818</u>	<u>107,948</u>	<u>(88,486)</u>	<u>(7,408)</u>	<u>(57)</u>	<u>(79)</u>	<u>190</u>	<u>31,926</u>

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

Consolidated statements of changes in equity

	Relating to the Company's shareholders							Total equity
	Share capital	Additional paid-in capital	Retained deficit	Treasury shares	Capital reserve for available for sale financial assets	Capital reserve for cash flow hedges	Capital reserve for transactions with a contr. Shareholder	
	Unaudited							
	Dollars thousands							
Balance as at July 1, 2010	10,351	108,852	(65,915)	(7,408)	(122)	-	190	45,948
Total comprehensive income (loss)	-	-	(3,223)	-	-	-	-	(3,223)
Share-based payment	-	90	-	-	-	-	-	90
Balance as at September 30, 2010	<u>10,351</u>	<u>108,942</u>	<u>(69,138)</u>	<u>(7,408)</u>	<u>(122)</u>	<u>-</u>	<u>190</u>	<u>42,815</u>
Balance as at January 1, 2010	\$ 7,518	\$ 107,522	\$ (60,666)	\$ (7,408)	\$ (86)	\$ 115	\$ -	\$ 46,995
Total comprehensive loss	-	-	(23,137)	-	(5)	(115)	-	(23,257)
Share-based payment	-	490	-	-	-	-	-	490
Rights issue (less issue expenses net of \$240 thousand)	2,833	927	-	-	-	-	-	3,760
Private issue (less issue expenses net of \$297 thousand)	9,467	(1,735)	-	-	-	-	-	7,732
Capital benefit from a transaction with a controlling shareholder	-	-	-	-	-	-	190	190
Balance as at December 31, 2010	<u>\$ 19,818</u>	<u>\$ 107,204</u>	<u>\$ (83,803)</u>	<u>\$ (7,408)</u>	<u>\$ (91)</u>	<u>\$ -</u>	<u>\$ 190</u>	<u>\$ 35,910</u>

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

Consolidated statements of cash flows

	For the nine months ended		For the three months ended		For the year ended
	September 30,		September 30,		December 31
	2011	2010	2011	2010	2010
	Unaudited				Audited
	In dollars thousands				
<u>Cash flows from operating activities</u>					
Loss	\$ (4,558)	\$ (8,326)	\$ (529)	\$ (3,077)	\$ (22,686)
Adjustments to reconcile net income (loss) to net cash provided by (used for) operating activities:					
Adjustments to the statement of income items:					
Depreciation and amortization	4,888	6,809	1,317	2,268	9,503
Impairment in fixed and intangible assets	-	133	-	133	6,260
Inventory write-off	467	738	142	72	3,065
Share-based payment	334	230	111	90	280
Loss (gain) on sale of property, plant and equipment	28	(31)	-	-	142
Deferred taxes, net	(223)	(2,491)	(94)	(872)	(2,643)
Change in employee benefits, net	(150)	(422)	(76)	(123)	(664)
Taxes on income	171	124	24	41	(20)
Financial expenses	1,176	1,059	542	516	1,452
	6,691	6,149	1,966	2,125	17,375
<u>Changes in items of operating assets and liabilities:</u>					
Decrease (increase) in trade receivables	(4,332)	5,075	4,616	4,112	5,258
Decrease (increase) in other receivables	(172)	714	240	793	924
Decrease (increase) in inventory	(1,278)	3,415	(3,020)	2,754	1,950
Increase (decrease) in trade payables	1,523	(6,061)	(835)	(5,067)	(3,178)
Increase (decrease) in other payable	(3,835)	(3,214)	41	(325)	(631)
	(8,094)	(71)	1,042	2,267	4,323
<u>Cash paid and received during the year for:</u>					
Interest paid	(1,032)	(1,059)	(384)	(516)	(1,482)
Interest received	21	-	7	-	30
Taxes paid	(171)	(124)	(24)	(41)	(171)
Taxes received	-	-	-	-	191
	(1,182)	(1,183)	(401)	(557)	(1,432)
Net cash used for operating activities	\$ (7,143)	\$ (3,431)	\$2,078	\$ 758	\$ (2,420)

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

Consolidated statements of cash flows

	For the nine months ended		For the three months ended		For the year ended
	September 30,		September 30,		December 31
	2011	2010	2011	2010	2010
	Unaudited				Audited
	In dollars thousands				
<u>Cash flows from investing activities</u>					
Purchase of fixed assets	(287)	(72)	(81)	(31)	\$ (111)
Purchase of intangible assets	(16)	(2)	(16)	-	(2)
Proceeds from sale of fixed assets	157	133	-	92	367
Net cash provided by (used for) investing activities	(146)	59	(97)	61	254
<u>Cash flows from financing activities</u>					
Short-term credit from banks, net	19	(8,796)	215	690	(8,052)
Repayment of long-term loans	(239)	(11,601)	(13)	-	(11,601)
Proceeds of long-term loans	3,800	20,000	-	-	20,000
Proceeds from a private placement, net	-	-	-	-	5,516
Proceeds from rights offering, net	-	3,813	-	-	3,760
Net cash provided by financing activities	3,580	3,416	202	690	9,623
<u>Increase (decrease) in cash</u>	(3,709)	44	2,183	1,509	7,457
<u>Balance of cash at beginning of year</u>	9,361	1,904	3,469	439	1,904
<u>Balance of cash at end of year</u>	\$ 5,652	\$ 1,948	\$ 5,652	\$ 1,948	\$ 9,361

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

Consolidated statements of cash flows

	For the nine months ended September 30,		For the three months ended September 30,		For the year ended December 31
	2011	2010	2011	2010	2010
	Unaudited				Audited
	In dollars thousands				
(A) Significant non cash activities					
Acquisition of operations					
Assets of the operations on the acquisition date:					
Inventory	-	-	-	-	1,896
Customer base	-	-	-	-	1,551
Order backlog	-	-	-	-	408
NB brand license	-	-	-	-	78
Goodwill	-	-	-	-	49
	-	-	-	-	3,982
Granting options in the framework of a rescheduling of loans	-	194	-	(8)	210
Acquisition of fixed assets	228	-	228	-	-

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

Notes to the interim consolidated financial statements

Note 1 – General

- a. These financial statements were prepared in a condensed format, as at September 30, 2011 and for the period of nine months then ended (hereinafter – Interim Consolidated Financial Statements). These statements should be studied in conjunction with the Company's annual financial statements as at December 31, 2010 and for the year then ended, and the notes accompanying them (hereinafter – the Annual Financial Statements).
- b. During 2010 the Company raised a total of \$9.8 million from its shareholders; it acquired operations in the field of "seamless" products and reorganized its debts vis-à-vis the banks, as follows:

During March 2010 the Company raised through a rights offering to its shareholders and a private placement, a total amount of \$4 million gross. In addition, on March 2, 2010, the Company signed an agreement with the banks regarding the reorganization of the credit lines and new liabilities to the banks; and on December 24, 2010 it signed an amendment to the final agreement. According to the amendment to the agreement with the banks, the Company must meet new financial covenants agreed with the banks.

On December 30, 2010, the Company signed a number of agreements in the framework of which it acquired, *inter alia*, operations in the fields of "seamless" products of Intimes Nouvelle Seamless Inc. (hereinafter: "Nouvelle") and an amount of \$5.8 million was invested in the Company by parties related to Nouvelle and by interested parties in the Company.

- c. During the periods of nine and three months ended September 30, 2011, and for the year ended December 31, 2010, the Company had losses of \$4,548 thousand, \$529 thousand and \$22,686 thousand, respectively. In addition during the periods of nine months ended September 30, 2011 and the year ended December 31, 2010 the Company had negative cash flows from operating activities of \$7,143 thousand and \$2,420 thousand, respectively. It should be stated that in the period of three months ended September 30, 2011, the Company had positive cash flows from operating activities of \$2,078 thousand.

Management's plans to improve its business condition, including the integration of Nouvelle's operations, establishing relationships with the new customers who were transferred to the Company, in the framework of the Nouvelle transaction, and continued activities to expand the customer base in Europe and the US, and this with a view to increase the level of sales. In addition, continued efforts to make the production floor more efficient and expand business with suppliers in the Far East.

Furthermore, according to the amendment to the agreement with the banks, from January 1, 2011 the Company must meet new financial covenants. Correct as of the date of signing the financial statements, the Company's management estimates that in the coming year the chances of meeting the financial covenants are more likely than not, i.e.: the chances are higher than 50%; although, there is no certainty that it will meet these financial covenants in the coming year, as meeting them is subject to the occurrence of future events.

Notes to the interim consolidated financial statements

Note 2 – Significant accounting principles

Form of preparation of interim consolidated financial statements

The interim consolidated financial statements are prepared in accordance with the generally accepted accounting principles for the preparation of financial statements for interim periods, as set forth in International Accounting Standard 34 – Financial Reporting for Interim Periods, and according to the provisions of the pronouncement under Chapter D of the Securities Regulations (Periodic and Immediate Reports) – 1970.

The significant accounting principles and methods of calculation implemented in the preparation of the interim consolidated financial statements are consistent with those implemented in the preparation of the annual financial statements, excluding the following:

IAS 1 – Presentation of the financial statements

According to the amendment, it is possible to present the movement between the opening balance and the closing balance for every component of other comprehensive income in the statement of changes in capital or in the context of the notes to the annual financial statements. Accordingly, the Company elected to present the above details in the statement of changes in shareholders' equity.

The amendment was implemented retrospectively starting January 1, 2011.

IAS 24 – Disclosures relating to a third party

The amendment to IAS 24 clarifies the definition of a related party so as to simplify the identity of the relationships with a related party and prevent a lack of consistency in implementing this definition. In addition, companies related to the government are given, in the framework of the amendment, partial exemptions in disclosures regarding transactions with the government and with other companies connected to the government.

The amendment has been implemented retrospectively as from January 1, 2011.

IAS 34 – Financing reporting for interim periods

In accordance with the amendment to IAS 34, disclosure requirements were added to the interim financial statements regarding circumstances that it is reasonable that they will affect the fair value and classification of the financial instruments, transfers of financial instruments between various levels in fair value and changes in classification of financial statements.

The amendment has been implemented retrospectively as from January 1, 2011.

First implementation of the amendment did not have an effect on the financial statements.

Notes to the interim consolidated financial statements

Note 2 – Significant accounting principles – contd.**Reclassification of development costs**

During the year the Company reclassified development expenses in the statement of income from cost of sales to development expense item so as to properly reflect the nature of the expenses.

Development expenses, net, which reflect the Company's investment in the development of products with technological changes, changes in marketing destinations and changes in use by the final customer are represented net of grants from the Chief Scientist. During the period of none and three months ended September 30, 2011 the participation of the Chief Scientist aggregated \$571 thousand and \$187 thousand respectively.

Disclosure to new IFRS Standards during the period prior to their implementation**IFRS 10 – Consolidated financial statements**

IFRS 10 (hereinafter - Standard 10) replaces IAS 27 regarding the accounting treatment of consolidated financial statements and includes the accounting treatment of structured entities which were handled in the past in SIC 12 Consolidation – special purpose entities.

Standard 10 does not include changes in consolidation procedures but changes the definition of existence of control for consolidation and includes a single model for consolidation purposes. According to Standard 10 in order that control can exist power and exposure is required or the right to variable returns from the investee company. Power is the ability to affect and direct the investee company's operations which significantly affect the return of the investor.

Standard 10 stipulates that on examining the existence of control, potential voting rights must only be taken into account if they are real, compared to IAS 27 before the amendment that stipulated that potential voting rights will be taken into account only they are immediately realizable, while disregarding management's intentions and financial ability to realize these rights.

In addition, Standard 10 stipulates that an investor can control even if he holds less than the majority of voting rights in the investee companies (effective control), and this contrary to the existing IAS 27 which enabled the choice of two models for the consolidation – the effective control model and the legal control model.

Standard 10 will be implemented retrospectively as from the financial statements for annual periods starting on January 1, 2013 or thereafter.

In the Company's opinion, Standard 10 is not expected to have a significant effect on the financial statements.

Notes to the interim consolidated financial statements

Note 2 – Significant accounting principles – contd.

IAS 27R – Separate financial statements

IAS 27R (hereinafter – Standard 27 amended) replaces IAS 27 and handles only separate financial statements. The existing provisions regarding the separate financial statements are unchanged in the context of Standard 27 amended.

IFRS 12 – Disclosure regarding rights in other entities

IFRS 12 (hereinafter – Standard 12) sets forth disclosure requirements regarding entities held by of the Company, including subsidiaries, joint arrangements, affiliated companies and structured entities. Standard 12 extends the disclosure requirements regarding considerations and assumptions which management used in determining the existence of control, joint control or significant influence in investee entities, and determining the type of joint arrangement. Standard 12 includes also disclosure requirements regarding significant investee entities.

These disclosures will be included in the Company's financial statements on the first adoption of the Standard.

IFRS 13 – Measurement of fair value

IFRS 13 (hereinafter – Standard 13) sets forth directives regarding the method of measuring fair value, to the extent that such measurement is required by the international standards. Standard 13 defines fair value as the price which would be received from the sale of an asset, or paid in transfer of a liability, in an orderly transaction between market participants on the measurement date. In addition, Standard 13 details the characteristics of market participants and states that the fair value will be based on the assumptions that the market participants will utilize. Moreover, Standard 13 states that the measurement of fair value will be based on the assumption that the transaction will take place in the principal market of the asset or liability or, in the absence of a principal market, in the most advantageous market.

Standard 13 determines that one must maximize the use of data which can be seen in the market compared to the use of data which cannot be seen the market. Moreover, Standard 13 sets forth a hierarchy of fair value in accordance with the source of the data used to determine the fair value:

- Level 1: Quoted prices (not adjusted) in an active market of identical assets and liabilities.
- Level 2: Data which is not quoted prices included in Level 1 that can be seen, directly or indirectly.
- Level 3: Data not based on market information which can be seen - (evaluation techniques without the use of market data which can be seen).

In addition, Standard 13 sets forth certain disclosure demands.

The new disclosures and the measurement of assets and liabilities of Standard 13 are required 'from here on' only regarding periods starting after the date of their implementation, starting from the financial statements for annual periods starting January 1, 2013 or thereafter. Early adoption is possible. These new disclosures do not apply to comparative figures.

These disclosures will be included in the Company's financial statements when first adopting the Standard.

Regarding the effect on the financial statements, in the Company's opinion Standard 13 is not expected to have a significant effect on the financial statements.

Notes to the interim consolidated financial statements

Note 2 – Significant accounting principles – contd.**IAS 19 (amended) – Employees benefits**

In June 2011 the International Accounting Standard Boards published IAS 19 (amended) (hereinafter – the Standard). The main amendments included in the Standard are:

- Actuarial profits and losses will be recognized only in other comprehensive income and will not be recorded to the statement of income.
- The "Strip" method which enabled the postponement of actuarial profits or losses is cancelled.
- Yield of the Plan's assets will be recognized in the statement of income based on the discount rate used in measuring liabilities due to employee benefits unconnected to the actual composition of the investment portfolio.
- The distinction between short-term employee benefits and long-term employee benefits will be based on the expected settlement date and not on the date on which the employee is entitled to the benefits.
- Past services cost stemming from changes in the Plan will be immediately recognized.

The Standard will be implemented retrospectively starting from the financial statements for annual periods starting January 1, 2013 or thereafter. Early adoption is possible.

It is the Company's opinion the Standard is not be expected to have a significant effect on the financial statements.

Note 3 – Seasonality

The Company's intimate apparel and sportswear products are not affected by seasonality. In the swimwear products, most of the Company's sales are carried during the months of December to May and consequently in the third quarter sales of swimwear are considerably lower. The results of operations should be studied considering this seasonality.

Note 4 – Non current assets held for sale

Further to Note 7d to the annual financial statements regarding the Company's management's decision to classify knitting machines, totaling \$2,005 thousand, from fixed assets to non-current assets held for sale, on March 3, 2011 the Company decided on the discontinuation of production in the Cut & Sew field in Israel - as detailed in Note 5a below. The Company took the decision to realize the production assets and started a process of locating a potential buyer. Consequently, the Company carried out a classification of the machines used for these operations, from fixed assets to non-current assets held for sale. During the period of report, some of these machines were sold. Correct as at September 30, 2011, the net realization price of the machines which were classified as non-current assets available for sale is \$3,221 thousand.

Notes to the interim consolidated financial statements

Note 5 – Significant events during the period of reporta. Discontinuation of production in the Cut & Sew field in Israel

On March 3, 2011, Company's management decided on the discontinuation of production in the Cut & Sew field in Israel. This decision is based on the decline in levels of production in Israel for this field, up to a minimum production at the end of 2010. The decline in production in Israel started due to the transfer of production lines abroad and due to the discontinuation of the production of losing products. The Company operates in the design, development, marketing and management of the Cut & Sew segment in Israel, where production is now concentrated in countries in the Far East.

b. Change of estimates in the lifespan of the knitting machines

In June 2011 the Company engaged with an external and independent evaluator, who is required to determine the balance of the lifespan of the knitting machines that the Company operates. The evaluator determined that the life span of some of the knitting machines is at least an additional 5 years from June 29, 2011. Consequently, the Company changed the balance of the lifespan of the knitting machines that it operates to five additional years, from the beginning of the third quarter of 2011.

c. Granting options to officers and other employees

On August 16, 2011 the Company's Board of Directors approved the granting of 82,000 option warrants which can be exercised to 82,000 ordinary shares of NIS 10 par value each to three officers and eight other employees of the Company, who are not interested parties in the Company and did not become interested parties in the Company after the granting. The allotment of the option warrants to offerees will be made according to an option plan for employees, officers and consultants of the Company. The exercise price of every option will stand at 3.8 dollars, being translated into NIS at the representative rate of exchange of the dollar on the day preceding the date of the allotment. The entitlement to exercise the options will be vested over a period of three years starting March 28, 2011, which is the date of first approval by the Board of Directors. On August 16, 2011, the Company's Board of Directors was required to re-approve the granting due to the request of the Stock Exchange to change the mechanism for determining the exercise price.

Correct as on the date of the statement, the actual granting of the options to the employees has not yet been effected.

Notes to the interim consolidated financial statements

Note 5 – Significant events during the period of report – contd.d. **Deregistration the Company's shares under the U.S. Securities Laws**

On September 2011, the Company submitted documents in the USA in order to deregister its shares under the U.S. Securities Laws, in such a way that on such deregistration the Company's obligation to report to the U.S Securities will be cancelled. As a result of this deregistration procedure, trading of the Company's shares will stop over-the-counter bulletin board in the USA (hereinafter: "OTCBB). It should be emphasized that the Company's shares will continue to trade on the Tel Aviv Stock Exchange.

Note 6 – Business segmentsa. **General**

The companies in the Group are engaged in two operating business segments:

Seamless apparel ("Seamless") - The design, development, production, and sale of intimate apparel and sportswear, using the "Seamless" method;

Knitted apparel (Cut & Sew) - The design, development, production and sale of intimate wear, swimwear and sportswear using the "Cut & Sew" method. The design is done mainly in Israel and the production is mainly done in Jordan and in the Far East, while the sale of the finished product is carried out mainly in the US and in Europe.

The Company's two operating segments are carried out in a number of main geographic regions in the world. In Israel, the Company's place of residence and of its subsidiaries, Hi-Tex, was founded by Tefron Ltd., and Macro Apparel Ltd. carry out the design, development, production and sale of intimate apparel, sportswear and swimwear. The subsidiaries Tefron U.S and Tefron England perform the marketing and selling operations.

The information that the Company reports according to the definitions of IFRS 8 is based on available financial information which is regularly reviewed and serves the Chief Operating Decision Maker in the Company (CODM) in order to make decisions regarding resources to be allotted to the segments and to evaluate the segments' performance. The Chief Operating Decision Maker in the Company is the CEO. Based on the criteria in IFRS 8 to determine reportable operating segments and the financial information available and reviewed by the Company's CEO, the Company decided that it operates in two reportable operating segments.

The results of the reportable segments represent the operative income attributed to the segment.

The financing of the Group (including financing costs and financing revenues) and taxes on income are managed on a group basis and do not related to the operating segments.

Notes to the interim consolidated financial statements

Note 6 – Business segments (contd.)**b. Reporting regarding operating segments**

	For the period of 9 months ended September 30, 2011			For the period of 9 months ended September 30, 2010		
	Seamless	Cut & Sew	Total	Seamless	Cut & Sew	Total
	Unaudited			Unaudited		
	Dollars thousands					
External revenues	70,200	16,685	86,885	39,490	29,219	68,709
Gross profit	10,068	3,729	13,797	519	4,209	4,728
Segment results	(3,120)	(602)	(3,722)	(7,088)	(1,826)	(8,914)
Financing expenses, net			(1,025)			(1,777)
Tax benefit			189			2,365
Loss			(4,558)			(8,326)

	For the period of 3 months ended September 30, 2011			For the period of 3 months ended September 30, 2011		
	Seamless	Cut & Sew	Total	Seamless	Cut & Sew	Total
	Unaudited			Unaudited		
	Dollars thousands					
External revenues	27,815	2,304	30,119	15,927	2,063	17,990
Gross profit (loss)	4,377	201	4,578	1,007	(358)	649
Segment results	415	(960)	(545)	(1,470)	(1,610)	(3,080)
Financing expenses			(73)			(869)
Tax benefit			89			872
Loss			(529)			(3,077)

