Cellcom Israel Ltd.
Form 20-F
March 18, 2019

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 20–F

REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

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

For the fiscal year ended December 31, 2018

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ____________ to ______________

OR

SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

Date of event requiring this shell company report …………………………….

Commission file number 001-33271

CELLCOM ISRAEL LTD.

(Exact name of Registrant as specified in its charter
and translation of Registrant's name into English)

ISRAEL

(Jurisdiction of incorporation or organization)

10 Hagavish Street, Netanya 4250708, Israel

(Address of principal executive offices)

Liat Menahemi Stadler, 972-52-9989595 (phone), 972-98607986 (fax), LIATME@cellcom.co.il, 10 Hagavish Street, Netanya 4250708, Israel

(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

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

Title of each class	Name of each exchange on which registered
Ordinary Shares, par value NIS 0.01 per share	New York Stock Exchange ("NYSE")

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

None

(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.

None

(Title of Class)

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

As of December 31, 2018, the Registrant had outstanding 116,196,729 Ordinary Shares, par value NIS 0.01 per share.

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

If this report is an annual or transition report, indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes No

Indicate by check mark whether the Registrant has (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the Registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files)

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer , or an emerging growth company. See definition of "large accelerated filer", "accelerated filer," and "emerging growth company" in Rule 12b-2 of the Exchange Act:

Large accelerated filer Accelerated filer Non-accelerated filer Emerging growth company

If an emerging growth company that prepares its financial statements in accordance with U.S. GAAP, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act

The term "new or revised financial accounting standard" refers to any update issued by the Financial Accounting Standards Board to its Accounting Standards Codification after April 5, 2012.

Indicate by check mark which basis of accounting the Registrant has used to prepare the financial statements included in this filing:

U.S. GAAP

International Financial Reporting Standards as issued by the International Accounting Standards Board

Other

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the Registrant elected to follow.

Item 17

Item 18

If this is an annual report, indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

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INTRODUCTION

In this annual report, “Cellcom,” the “Company,” “we,” “us” and “our” refer to Cellcom Israel Ltd. and its subsidiaries. The terms “NIS” refers to new Israeli shekel, and “dollar,” “USD” or “$” refers to U.S. dollars. The term "Companies Law" shall mean the Israeli Companies Law of 1999.

Presentation of Financial and Share Information

We prepare our consolidated financial statements in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board ("IASB").

Unless we indicate otherwise, U.S. dollar translations of the NIS amounts presented in this annual report are translated for the convenience of the reader using the rate of NIS 3.748 to $1.00, the representative rate of exchange as of December 31, 2018 as published by the Bank of Israel. The translation is for the convenience of the reader only, and it does not represent the fair value of the translated assets and liabilities.

Trademarks

We have proprietary rights to trademarks used in this annual report which are important to our business. We have omitted the “®” and “™” designations for certain trademarks, but nonetheless reserve all rights to them. Each trademark, trade name or service mark of any other company appearing in this annual report belongs to its respective holder.

Industry and Market Data

This annual report contains information about our market share, market position and industry data. Unless otherwise indicated, this statistical and other market information is based on statistics prepared by the Ministry of Communications of Israel, Brandman Marketing Research and Consultancy Institute, Sapio Research & Development, Pyramid Research, and Meida Shivuki C.I. (survey institute). Industry publications generally state that the information they contain has been obtained from sources believed to be reliable, but the accuracy and completeness of such information is not guaranteed. We have not independently verified the accuracy of market data and industry forecasts contained in this annual report that were taken or derived from these industry publications.

Special Note Regarding Forward-Looking Statements

We have made statements under the captions “Item 3. Key Information - D - Risk Factors,” “Item 4 – Information on the Company,” “Item 5. Operating and Financial Review and Prospects,” and in other sections of this annual report that are forward-looking statements. In some cases, you can identify these statements by forward-looking words such as “may,” “might,” “will,” “should,” “expect,” “plan,” “anticipate,” “believe,” “estimate,” “predict,” “potential” or “continue,” the negati terms and other comparable terminology. These forward-looking statements, which are subject to risks, uncertainties and assumptions about us, may include projections of our future financial performance, our anticipated growth strategies and anticipated trends in our business. These statements are only predictions based on our current expectations and projections about future events. There are important factors that could cause our actual results, level of activity, performance or achievements to differ materially from the results, level of activity, performance or achievements expressed or implied by the forward-looking statements, including those factors discussed under the caption entitled “Item 3. Key Information - D. Risk Factors.” You should specifically consider the numerous risks outlined under “Item 3. Key Information - D. Risk Factors.”

Although we believe the expectations reflected in the forward-looking statements contained in this annual report are reasonable, we cannot guarantee future results, level of activity, performance or achievements. Moreover, neither we nor any other person assumes responsibility for the accuracy and completeness of any of these forward-looking statements. We assume no duty to update any of these forward-looking statements after the date of this annual report to conform our prior statements to actual results or revised expectations, except as otherwise required by law.

PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISORS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

A. SELECTED FINANCIAL DATA

You should read the following selected consolidated financial data in conjunction with the section of this annual report entitled “Item 5. Operating and Financial Review and Prospects” and our consolidated financial statements, the notes thereto, the independent registered public accounting firms’ report and the convenience translation of the consolidated financial statements as of and for the year ended December 31, 2018 into U.S. dollars solely for the convenience of the reader, included elsewhere in this annual report.

The selected data presented below under the captions “Income Statement Data” and “Statement of Financial Position Data” for, and as of the end of, each of the years in the five-year period ended December 31, 2018, are derived from the consolidated financial statements of Cellcom Israel Ltd. and subsidiaries. The consolidated financial statements as of December 31, 2017 and 2018, and for each of the years in the three-year period ended December 31, 2018, and the report thereon, are included elsewhere in this annual report. Data for 2015 and 2014, and the selected consolidated balance sheet data as of December 31, 2016, 2015 and 2014, have been derived from our previously reported audited consolidated financial statements, which are not included in this annual report. The selected financial data should be read in conjunction with our consolidated financial statements and accompanying notes and “Operating and Financial Review and Prospects” appearing in Item 5 of this annual report, and are qualified entirely by reference to such consolidated financial statements.

The information presented below under the caption "Other Data" contains information that partly is not derived from the financial statements.

For your convenience, the following tables also contain U.S. dollar translations of the NIS amounts presented at December 31, 2018, translated using the rate of NIS 3.748 to $1.00, the representative rate of exchange on December 31, 2018 as published by the Bank of Israel.

	Year Ended December 31,					
	2014	2015	2016	2017	2018	2018
	(In NIS millions, except where indicated otherwise)					(In US$ millions)
Income Statement Data:						
Revenues	4,570	4,180	4,027	3,871	3,688	984
Cost of revenues	2,727	2,763	2,702	2,680	2,661	710
Selling and marketing expenses	672	620	574	479	567	151
General and administrative expenses	463	465	420	426	360	96
Other (income) expenses, net	46	22	21	(11)	26	7
Operating profit	662	310	310	297	74	20
Financing expense, net	198	177	150	144	144	39
Tax benefit(tax on Income)	110	36	10	40	(6)	(2)
Net income (loss)	354	97	150	113	(64)	(17)
Basic earnings (loss) per share (in NIS)	3.51	0.95	1.47	1.11	(0.58)	(0.15)
Diluted earnings(loss) per share (in NIS)	3.48	0.95	1.47	1.10	(0.58)	(0.15)
Weighted average ordinary shares used in calculation of basic earnings per share (in shares)	99,924,306	100,589,458	100,604,578	100,654,935	107,499,543	107,499,543
Weighted average ordinary shares used in calculation of diluted earnings per share (in shares)	100,706,282	100,589,530	100,698,306	100,889,661	107,499,543	107,499,543

(*) The results at and for the years 2017 and 2018, include the impact of the adoption of IFRS 15 with effect as of January 1, 2017.

Statement of Financial Position Data:						
Cash and cash equivalents	1,158	761	1,240	527	1,202	321
Working capital	837	625	1,074	692	1,269	339

Total assets	7,240	6,278	6,662	6,087	6,749	1,800
Total equity	1,092	1,185	1,340	1,441	1,677	448
Other Data:						
Adjusted EBITDA(1)	1,282	872	858	853	660	176
Capital expenditures	487	396	382	550	647	173
Dividends declared per share	-	-	-	-	-	-
Net cash from operating activities	1,557	836	781	774	770	205
Net cash used in investing activities	(350)	(96)	(364)	(644)	(631)	(168)
Net cash from (used in) financing activities	(1,106)	(1,136)	62	(843)	537	143
Cellular Subscribers (in thousands)(2)	2,967	2,835	2,801	2,817	2,851	2,851
Churn rate of cellular subscribers(4)	44.0%	42.0%	42.4%	45.8%	43.2%	43.2%
Cellular ARPU (in NIS)(5)	72	65	63	57	51	14
Internet customers (households) (end of period) (in thousands)(3)		95	156	222	269	269
TV customers (households) (end of period) (in thousands) (3)		63	111	170	219	219

(1) Adjusted EBITDA is a non-IFRS measure and is defined as income before financing income (expenses), net; other income (expenses), net (excluding gain from the sale of a subsidiary and expense related to employee retirement plans); income tax; depreciation and amortization and share based payments. We present adjusted EBITDA as a supplemental performance measure because we believe that it facilitates operating performance comparisons from period to period and company to company by backing out potential differences caused by variations in capital structure (most particularly affecting our interest expense given our significant debt), tax positions (such as the impact on periods or companies of changes in effective tax rates or net operating losses) and the age of, and depreciation expenses associated with property, plant and equipment. Adjusted EBITDA should not be considered in isolation or as a substitute for operating income or other statement of operations or cash flow data prepared in accordance with IFRS as a measure of our profitability or liquidity. Adjusted EBITDA does not take into account our debt service requirements and other commitments, including capital expenditures, and, accordingly, is not necessarily indicative of amounts that may be available for discretionary uses. In addition, adjusted EBITDA, as presented in this annual report, may not be comparable to similarly titled measures reported by other companies due to differences in the way that these measures are calculated.

The following is a reconciliation of net income to adjusted EBITDA:

	Year Ended December 31,					
	2014	2015	2016	2017	2018	2018
	(In NIS millions)					(In US$ millions)
Net income (loss)	354	97	150	113	(64)	(17)
Financing expense, net	198	177	150	144	144	38
Other expenses (income),net (excluding expense related to employee retirement plans and gain from the sale of a subsidiary);	7	(3)	8	(1)	-	-
Tax benefit (tax on income) income	110	36	10	40	(6)	(2)
Depreciation and amortization	610	562	534	555	584	156
Share based payments	3	3	6	2	2	1
Adjusted EBITDA	1,282	872	858	853	660	176

(2) Cellular subscriber data refers to active subscribers. We use a six-month method of calculating our cellular subscriber base, which means that we add post-paid subscribers to our subscriber base upon their joining our services and prepaid subscribers upon charging a prepaid card and we deduct subscribers from our subscriber base after six months of no revenue generation and activity on our network and no data usage or less than NIS 1 of accumulated revenues for M2M (machine to machine) subscribers. The six-month method is, to the best of our knowledge, consistent with the methodology used by other cellular providers in Israel. The 2017 cellular subscriber base includes subscribers added as part of our purchase of the operations of an Israeli Mobile Virtual Network Operator, or MVNO, during the third quarter of 2017. As of the third quarter of 2018, we add M2M subscribers to the cellular subscriber base only upon first use instead of at the time of joining our service as was done until the change. This change did not have a material effect on M2M prior subscriber data.

(3) Internet and TV customers refer to active subscribers. Internet households receive end-to-end internet service, including infrastructure (based on the wholesale landline market) and connectivity services.

(4) Churn rate is defined as the total number of voluntary and involuntary permanent deactivations of cellular subscribers in a given period expressed as a percentage of the number of cellular subscribers at the beginning of the period. Involuntary permanent deactivations relate to cellular subscribers who have failed to pay their arrears for the period of six consecutive months. Voluntary permanent deactivations relate to cellular subscribers who terminated their use of our cellular services. Churn rate data is excluding the above mentioned removals of subscribers.

(5) Average monthly revenue per cellular subscriber (ARPU) is calculated by dividing revenues from cellular services for the period by the average number of cellular subscribers during the period and by dividing the result by the number of months in the period. Revenues from inbound roaming services and hosting and network sharing services are included even though the number of cellular subscribers in the equation does not include the users of those roaming, hosting and network sharing services. Inbound roaming services, hosting and network sharing services are included because ARPU is meant to capture all service revenues generated by a cellular network. Revenues from repair services pursuant to a monthly subscription, or Subscription Repair Services, are included because they represent recurring revenues generated by cellular subscribers, but revenues from sales of handsets (which for purposes of this report may include other types of cellular end user equipment, such as tablets), non-subscription repair services carried out on a random basis, or Random Repair Service, and other services are not included. We and industry analysts treat ARPU as a key performance indicator of a cellular operator because it is the closest meaningful measure of the contribution to service revenues made by an average subscriber.

We have set out below the calculation of cellular ARPU for each of the periods presented:

	Year Ended December 31,					
	2014	2015	2016	2017	2018	2018
	(In NIS millions, except number of subscribers and months)					(In US$ millions)
Revenues	4,570	4,180	4,027	3,871	3,688	984
less revenues from equipment sales	1,005	1,048	994	952	904	241
less other revenues*	941	869	881	949	1,061	283
Revenues used in cellular ARPU calculation	2,624	2,263	2,152	1,971	1,723	460
Average number of cellular subscribers	3,034,946	2,898,987	2,832,407	2,797,341	2,826,013	2,826,013
Months during period	12	12	12	12	12	12
Cellular ARPU (in NIS, per month)	72	65	63	57	51	14

* Other revenues include revenues from other communications services mainly fixed-line revenues and repair services.

B. CAPITALIZATION AND INDEBTEDNESS

Not applicable.

C. REASONS FOR THE OFFER AND USE OF PROCEEDS

Not applicable.

D. RISK FACTORS

We believe that the occurrence of any one or some combination of the following factors could have a material adverse effect on our business, financial condition or results of operations.

Risks Related to our Business

We operate in a heavily regulated industry, which can harm our results of operations. Regulation in Israel has materially adversely affected our results.

A substantial part of our operations is subject to the Israeli communications laws and the licenses for the provision of different telecommunications services that we received from the Ministry of Communications in accordance with the Communications Law. The interpretation and implementation thereof are not certain and subject to change and disagreements have arisen and may arise in the future between the Ministry of Communications, or MOC, and us. The Communications Law and regulations thereunder grant the Ministry of Communications extensive regulatory and supervisory authority with regard to our activities. The MOC may modify our licenses without our consent and in a manner that could limit our freedom to conduct our business and harm our results of operations. Frequent changes, or changes made or on a timetable we cannot meet, to our licenses and legislation can increase the risk of noncompliance with our licenses or violation of such legislation and our exposure to lawsuits and regulatory sanctions. The MOC has the authority to impose substantial sanctions in the event of a breach of our licenses or the applicable laws and regulations and the authority to revoke them, in case we materially violate their terms.

Our licenses are limited in time and may be extended upon our request to the Ministry of Communications and its confirmation that we have complied with the provisions of our license and the applicable law, have continuously invested in the improvement of our service and network and have demonstrated the ability to do so in the future.

Our operations are also subject to the regulatory and supervisory authority of other Israeli regulators which have the authority to impose criminal and substantial administrative sanctions against us.

Further, our business and results of operations could be materially and adversely affected by new legislation and decisions by regulators or the courts that:

- approve the annulment or further relaxation of the structural separation requirements imposed on the Bezeq communications group, given its monopolistic or duopolistic powers in most areas in which we compete, and also on the Hot communications group (though to a lesser degree, given that Hot already has substantial leniencies despite its monopolistic and duopolistic powers), especially if carried out before an effective landline wholesale market, which includes both telephony and infrastructure, is effected on both Bezeq's and Hot's infrastructure; set unfavorable regulation, including high tariffs for wholesale services, increasingly so in light of the rapidly growing demand for data capacity for both internet and television services; or insufficient mechanisms to prevent Bezeq and Hot from reducing their retail tariffs and thereby reducing the difference between the wholesale and retail tariffs ("margin squeeze"), or fail to enforce regulation with respect to the landline wholesale market resulting in our continued inability to use additional wholesale services. See also "– We face intense competition in all aspects of our business" below and "Item 4. Information on The Company – B. Business Overview "-Competition";

- award our competitors certain benefits and leniencies not available to us, including through waiving, easing or not enforcing requirements set in their licenses, or not making similar demands or not imposing similar restrictions or any regulation, for example, on foreign participants in the TV market. See also "Item 4. Information on the Company – B. Business Overview – Competition", "– Government Regulations – Cellular Segment" and thereunder: – Mobile Virtual Network Operators" and "Government Regulations – Fixed-line Segment";

- do not renew our licenses (or renew them on terms that are not favorable to us);

- do not renew the allocation of our frequencies (where applicable) or limit our usage thereof or demand that we return frequencies allocated to us or not allow us to obtain additional frequencies, as such become necessary, or do so under unfavorable terms, or demand that we change frequencies on an unreasonable timetable or bear the costs of such an exchange;

- publish frequencies tenders before we are in need of additional frequencies or before we have the means to participate in such tenders, or set deployment requirements for our network, using such new frequencies, given the substantial investments it would entail, without regard to our financial situation; see "As a result of substantial and continuing changes in our regulatory and business environment, our operating results, profitability and cash flow have decreased significantly in the past several years, with a loss for 2018. Further decline may adversely affect our financial condition" and "We may be adversely affected by the significant technological and other changes in the telecommunications industry "below and "Item 4. Information on the Company – B. Business Overview — Network and Infrastructure – Cellular Segment – Frequencies";

- allow additional competitors to enter the cellular market as 5G operators, which may further increase the competition in the market;

- impose new safety or health-related requirements;

- impose additional restrictions or requirements with respect to the construction and operation of cell sites or the networks;

- limit or prevent our ability to cooperate in deploying landline infrastructure with other operators or refuse to approve our recently announced investment in IBC Israel Broadband Company (2013) Ltd., or IBC. See also "Item 4. Information on the Company – B. Business Overview – Network and Infrastructure – Fixed-line Segment – Fixed-line Infrastructure – Investment in IBC";

- impose restrictions or demand we meet additional requirements on the provision of services or products we provide or regulate or otherwise intervene with the terms under which we advertise, market, price (including changes thereof) or provide them to our subscribers, credit terms, including in respect of existing agreements;

- allow other operators or other parties to provide services previously provided only by us to our subscribers;

- set higher service standards or costly requirements relating to the service we provide our customers, both in relation to our network quality and coverage and our customer service, including response times at our call centers;

- set a timetable for the implementation of new requirements in our license or other legislation which we cannot meet;

- impose a stricter policy or set stricter regulation with respect to privacy protection, such as with regard to data protection, collection, amelioration, segmentation or usage of data, including for commercial activities by us or for the benefit of third parties;

- impose regulation on our "over-the-top", or OTT, TV services, including the requirement to finance original productions, imposing or allowing unfavorable or discriminatory terms for the usage of the digital terrestrial television (DTT) broadcasting in Israel or applying such regulation to us and not to other OTT TV providers. See "– Item 4. Information on the Company – B. Business Overview – Government Regulations   Fixed-line Segment – OTT TV"; and

- limit or prohibit the renewal of our licenses and allocation of additional frequencies to us, as we are included in the list of concentrated entities (being a subsidiary of Discount Investment Corporation Ltd., or DIC) published annually according to the Law for the Promotion of Competition and the Mitigation of Concentration, or the Concentration Law.

If we fail to compensate for lost revenues, increased expenses (objectively or in comparison to our competitors) or additional investments resulting from past or future legislative or regulatory changes with alternative sources of income or otherwise, our results of operations may be materially adversely affected.

We face intense competition in all aspects of our business.

The Israeli telecommunications market is highly competitive in many of its elements. The competition level has increased substantially in recent years, following the entry of additional competitors and regulatory changes alleviating entry barriers and transfer barriers. We entered the TV market through our OTT TV service in December 2014 and the landline infrastructure market, through the landline wholesale market, in the first half of 2015, and in 2018 we commenced deployment of an independent fiber-optic infrastructure. In the other markets we operate in and specifically in the cellular market, price competition and erosion, high churn rate and high subscriber acquisition costs continue to materially affect our and other mobile network operators', or MNOs', revenues and profitability. The current level of competition in all the markets in which we operate and aggressive price plan offerings by our competitors may continue. See also the "Competition" section under “Item 4. Information on the Company - B. Business Overview","—Competition – Fixed-line Segment– Internet infrastructure and Connectivity Business" and "–Telephony Business". Should the current level of competition continue, it will continue to adversely affect our results of operations. Any of the following developments materializing in our market, may result in increased competition and further materially adversely affect our profitability:

- tariffs maintained at their current level or decreasing even further, including as part of a bundle;

- an ineffective landline wholesale market, including the de facto exclusion of telephony wholesale services, services provided not in line with the wholesale market criteria and not enforced by the MOC; unfavorable pricing harming our ability to provide competitive bundles and compete with the Hot and Bezeq groups, or change of current regulation to a less favorable one, given our dependence on the landline wholesale market in supplying our landline infrastructure services; or further escalation of the competition by Bezeq and Hot, given their dominance in the landline market, especially if the structural limitations on these groups are alleviated before an effective landline wholesale market is in effect. See also "Item 4. Information on The Company –B. Business Overview – Government Regulations – Fixed-line Segment – Landline";

- annulment or further relaxation of the structural separation imposed on each of the Bezeq and Hot groups or further consolidation of Bezeq's subsidiaries and their operations as it will provide the Bezeq and Hot groups a competitive advantage, given their dominance in the landline telephony and infrastructure markets and TV market. More so, in respect of our triple and quatro offering, given the de facto creation of a unified company by Bezeq's subsidiaries with the strong financial support of Bezeq. See also "Item 4. Information on The Company –B. Business Overview – Competition - Communications groups and structural separation"; "-Government Regulations – Fixed-line Segment – Landline";

- entrance of new competitors, including major global and local companies, such as Netflix, Amazon and other OTT participants in the TV market, to any of the markets we operate in, or complementary services becoming competitive to our services, or the entry of existing competitors to additional markets or segments where they are currently not or less active, or as a result of regulatory changes, allowing other operators to provide services currently provided only by us to our subscribers. See "Item 4. Information on The Company –B. Business Overview — Competition";

- our failure to deploy widespread landline infrastructure or turn IBC into a widespread landline infrastructure provider from which we can procure such service or enter into cooperation to use such infrastructure with an operator which owns such infrastructure, given the growth of our TV and internet services, especially if one of our competitors which currently does not own such infrastructure deploys such infrastructure or enters into such cooperation. Further, this may limit our broadband bandwidth offering in comparison to our competitors, since currently our offering of such service is mainly dependent on the landline wholesale market services, See "Item 4. Information on the Company –B. Business Overview — Competition – Fixed-Line Segment";

- our inability or failure to purchase additional frequencies or to purchase frequencies in an amount equal to our competitors, or to make the necessary investments in our networks or in our business in general, in order to maintain our competitive standing, given our financial situation or otherwise. See "- As a result of substantial and continuing changes in our regulatory and business environment, our operating results, profitability and cash flow have decreased significantly in the past several years, with a loss for 2018. Further decline may adversely affect our financial condition" above and "We may be adversely affected by the significant technological and other changes in the telecommunications industry" below;

- regulatory or technological changes, such as implementation of an electronic SIM (e-SIM) in cellular end-user equipment, facilitating even further transfer of customers among operators;

- the continued increased competition in the handsets market may result in decreased handset sales. See also "-We may not be able to maintain current handsets sales revenues and profitability." below and "Item 4. Information on The Company –B. Business Overview – Competition – Cellular Segment";

- some of our competitors may be able to obtain better access and terms of engagement with international suppliers or foreign carriers, than we do, due to their affiliation with international groups; or

- if our services are adversely affected by, or we are required to bear the costs of, a frequencies change, which do not affect our competitors. See "We may be adversely affected by the significant technological and other changes in the telecommunications industry" below.

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As a result of substantial and continuing changes in our regulatory and business environment, our operating results, profitability and cash flow have decreased significantly in the past several years, with a loss for 2018. Further decline may adversely affect our financial condition.

Our operating profit in 2018 was NIS 74 million ($20 million), a decrease of 75.1% from NIS 297 million ($79 million) in 2017 and a decrease of 76.1% from NIS 310 million in 2016. We recorded a loss in 2018 of NIS 64 million ($ 17 million), compared to net income of NIS 113 million ($30 million) in 2017 and a net income of NIS 150 million in 2016. The Company's net cash from operating activities in 2018 amounted to NIS 770 million ($205 million), a decrease of 0.5% from NIS 774 million ($207 million) in 2017 and a decrease of 1.4% from NIS 781 million ($208 million) in 2016. The principal factor leading to the continued decline in our operating results over the past several years has been the intense competition resulting largely from regulatory developments intended to enhance competition in the Israeli telecommunications market. These developments have caused, over the past several years, significant erosion in the prices charged for the provision of cellular services and a decrease from equipment sales.

As our business environment continues to be characterized by increased competition in the various markets in which we operate, these factors may continue to negatively impact our business, which may further adversely affect our results of operations and financial condition – that being more volatile than our competitors, due to our substantially larger amount of debt. Other impacts may include the need to reduce investments, in absolute terms and in comparison to our competitors, which may harm our competitive standing and potential future growth, . adversely affect our ability to raise additional debt and refinance our existing debt or adversely affect the terms and price of such debt raising, which in turn may further adversely affect our financial condition and may require equity capital raising, if possible. See also "- Our substantial debt increases our exposure to market risks, may limit our ability to incur additional debt that may be necessary to fund our operations and could adversely affect our financial stability" below.

We may not be able to obtain permits to construct and operate cell sites.

We depend on our network of cell sites to maintain and enhance network coverage for our cellular subscribers. We also deploy and operate microwave sites as part of our transmission network. The construction and operation of these various facilities are highly regulated and require us to obtain various consents and permits.

We have experienced difficulties in obtaining some of these consents and permits, particularly in obtaining building permits for cell sites from local planning and building authorities. As of December 31, 2018, we operated a small portion of our cell sites without building permits or applicable exemptions and approximately 33% of our cell sites without building permits in reliance on an exemption from the requirement to obtain a building permit, mainly for radio access devices. Such reliance had been challenged and under an interim order issued by the Supreme Court in September 2010, was reduced to replacing or relocating existing radio access devices under certain conditions. In October 2018, regulations setting procedures for the construction, changes and replacement of radio access devices exempt from building permits were enacted. Although these regulations reflect previous judicial limitations placed upon our ability to make changes and replace radio access devices, they also introduce a new licensing procedure that may further reduce our ability to construct new radio access devices based on such exemption. This may adversely affect our existing networks and our networks' build out. In addition, the Ministry of Justice expressed an opinion that such regulations and the exemption do not relate to the radio access devices' ancillary equipment. The Ministry of Justice is expected to publish further instructions in the matter. The exclusion of the ancillary equipment from the exemption, if adopted, could adversely affect our existing networks and our networks' build out. For additional details see "-"Item 4.B – Business Overview – Government Regulations – Cellular Segment – Permits for Cell Site Construction".

Additionally, District Court rulings adopted a narrower interpretation of 'rooftops' to which the exemption may be applied.

We also rely on the exemption for our rooftop microwave sites and signal amplifiers (known as 'repeaters'). It is unclear whether other types of repeaters require a building permit.

In addition, we may be operating a significant number of our cell sites in a manner that is not fully compatible with the building permits issued for these cell sites, which may, in some cases, also constitute grounds for termination of our lease agreements for those sites or claims for breach of such agreements.

Pursuant to the Israeli Non-Ionizing Radiation Law, 2006, the granting or renewal of an operating permit by the Commissioner of Environmental Radiation at the Ministry of Environmental Protection of Israel, or the Commissioner, for a cell site or other facility is subject to the receipt of a building permit or an exemption from such a permit.

Several local planning and building authorities are claiming that Israeli cellular operators may not receive building permits, in reliance on the Israeli National Zoning Plan 36, or the Plan, which regulates cell site construction and operation, for cell sites operating in frequencies not specifically detailed in the frequencies charts attached to the Plan and have refused to provide a building permit in a number of cases. Following conflicting district court decisions regarding this claim, the matter is expected to be decided by the Supreme Court. Some of the frequencies to which we may be required to transfer according to the MOC's instruction (see "We may be adversely affected by the significant technological and other changes in the telecommunications industry" below) are not specifically detailed in the Plan. Most of our cell sites and many cell sites operated by other operators also operate in frequencies not specifically detailed in the Plan.

Operation of a cell site or other facility without a building permit or operating permit or not in accordance with the permits or other legal requirements may subject us and our officers and directors to criminal, administrative and civil liability, to eviction orders in respect of the cell sites in breach, revocation or suspension of the operating permit, as well as to withholding the grant of operating permits to additional cell sites or demolition orders. As a result, we may be required to relocate cell sites to less favorable locations or stop operation of cell sites.

If we are unable to obtain or rely on exemptions from obtaining or to renew building or other consents and permits for our existing cell sites or other facilities, or if the Plan is changed to include additional restrictions and requirements on the construction and operation of cell sites or should the Supreme Court rule against the Company regarding the claim in relation to frequencies not specifically detailed in the Plan, it could adversely affect our existing network and its build-out, delay the deployment of our 4G network and future generations, negatively affect the extent, quality and capacity of our network coverage and our ability to continue to market our products and services effectively, all of which may have a material adverse effect on our results of operations and financial condition.

For additional details see "Item 4.B – Business Overview – Government Regulations – Cellular Segment – Permits for Cell Site Construction".

We may be required to indemnify certain local planning and building committees in respect of claims against them.

Under the Israeli Planning and Building Law, 1965, by approving a building plan, local planning and building committees may be required to compensate for depreciation of properties included in or neighboring the approved plan.

As a precondition to obtaining a cell site construction permit from a planning and building committee, we are required to provide a letter to the committee indemnifying it for possible depreciation claims and have provided hundreds of such indemnification letters to local planning and building committees. Calls upon our indemnification letters may have a material adverse effect on our financial condition and results of operations. We may also decide to demolish or relocate existing cell sites to less favorable locations or not at all, due to the obligation to provide indemnification. As a result, our existing service may be impaired or the expansion of our network coverage could be limited.

Alleged health risks relating to non-ionizing radiation generated from cell sites and cellular devices may harm our prospects.

Handsets, accessories and various types of cell sites are known to be sources of non-ionizing radiation emissions and are the subject of an ongoing public debate and concern in Israel. Radio frequency electromagnetic fields were classified by the International Agency for Research on Cancer (an agency of the World Health Organization) as possibly carcinogenic to humans (Group 2B), based on an increased risk for glioma, a malignant type of brain cancer associated with wireless phone use, and research is being conducted in regards to cellular handsets use and cancer and other health risks. The Israeli Ministry of Health published recommendations to take precautionary measures when using cellular handsets, and increasing awareness of the possible risks of cellular phones usage, reducing usage thereof and introducing precautionary measures were the subject of several bills in recent years. While, to the best of our knowledge, the handsets that we market comply with the applicable legislation that relate to acceptable "specific absorption rate," or SAR, levels, we rely on the SAR levels published by the manufacturers of these handsets and do not perform independent inspections of the SAR levels of these handsets. As the manufacturers' approvals refer to a prototype handset, we have no information as to the actual level of SAR of the handsets throughout the lifecycle of the handsets, including in the case of handset repair. See also "Item 4. Information on the Company – B. Business Overview – Government Regulations – Cellular Segment – Handsets".

Health concerns regarding cell sites have caused us difficulties in obtaining permits for cell site construction and obtaining or renewing leases for cell sites and even resulted in unlawful sabotage of a small number of cell sites and prompted proposed legislation aimed at increasing the minimum distance permitted between cell sites and certain institutions. Formal positions adopted by various Israeli government ministries with respect to radiation safety, include the 2009 position that cell sites constructed pursuant to a building permit are preferable to radio access devices, and that utilizing a cellular network to provide advanced services that can be provided through a landline network is not justified in light of the preventive care principle set forth in the Israeli Non-Ionizing Radiation Law.

If health concerns regarding non-ionizing radiation increase further, or if adverse findings in studies of non-ionizing radiation are published, non-ionizing radiation levels are found to be higher than the standards set for handsets and cell sites, we may be subject to health-related claims for substantial sums. Consumers may also be discouraged from using cellular handsets and regulators may impose additional restrictions on the construction and operation of cell sites or handset and accessories marketing and usage. As a result, we may experience increased difficulty in constructing and operating cell sites and obtaining leases for new cell site locations or renewing leases for existing locations, or be exposed to property depreciation claims; and we may lose revenues due to decreasing usage of our services and be subject to increased regulatory costs. We have not obtained insurance for these potential claims. An adverse outcome or settlement of any health-related litigation against us or any other provider of cellular services could have a material adverse effect on our results of operations, financial condition or prospects.

The unionizing of our employees may impede necessary organizational and personnel changes, result in increased costs or disruption to our operation.

In 2015, we entered into the first collective employment agreement with our employees' representatives and the Histadrut, an Israeli labor union, for a term of 3 years and in 2018 we entered into a new collective employment agreement for an additional 3 year term (2018-2020). The agreements have consistently increased our employment costs. The agreement defines employment policy and terms in various aspects, including payments to the employees, procedures relating to manning a position, change of place of employment and dismissal, including management's and the employees' representative's respective authority with regards to each. As a result, our day-to-day operations and our ability to execute organizational and personnel changes is more limited, cumbersome, costly and lengthy, as reflected in the voluntary retirement plans carried out in 2014 – 2016 and 2018, and requires more management attention that would otherwise be available for our ongoing business. In January 2019, the Histadrut announced a labor dispute at the Company, regarding the Company's intention to dismiss approximately 250 employees of the Company and failure to agree on other streamlining measures with the employees' union that do not include involuntary termination of employment. Under the announcement, the Company's employees would be entitled to take organizational steps (including a strike). We are negotiating a new collective employment agreement with our employees' representatives and the Histadrut but cannot guarantee the outcome of such negotiations.

Disagreements with the employees' representatives, may trigger work stoppages or other disruptions to our operation and an adverse impact on our services or customer service, changes may fail to be executed or be executed in a materially different way than planned, resulting in substantially lower savings than expected or requiring materially increased employment costs. Increased costs, inability or limited ability to make organizational and personnel changes, as well as work stoppages or other disruption to our operations and limitations on management's discretion, may damage the efficiency and quality of our operations, and may lead to damage to our reputation, increased customer churn, loss of market share and reduced profitability.

We are exposed to, and currently are engaged in, a variety of legal proceedings, including class action lawsuits.

We provide services to millions of subscribers on a daily basis. As a result of the scope and magnitude of our operations, as well as the multitude of pricing plans for stand-alone and bundles of services, the large amount of usage data our information systems need to process and record with relation to our subscribers according to their respective pricing plans, the frequent and multiple changes to our operation and pricing plans due to regulatory changes or in response to the changing market conditions, and the involvement of thousands of sales and customer service representatives in the sale process and after sale contacts with our existing or prospective customers - all increasing the risk of discrepancies occurring between a pricing plan and the information processed by our internal information systems or inadequate information provided, despite our continued efforts to the contrary - we are subject to the risk of a large number of lawsuits, including class action suits by consumers and consumer organizations. These actions are costly to defend and could result in significant judgments against us, which may materially and adversely affect our financial results. Recent years were characterized by a substantial increase in the number of purported class actions filed and approved in Israel, the greater involvement of consumer organizations and the Attorney General. In addition to eight class actions approved against us to date, we have entered into several settlement agreements, mostly for immaterial sums, and are currently engaged in dozens of purported class action suits as a defendant, many of which are for substantial amounts. For a summary of certain material legal proceedings against us, see “Item 8 – Financial Information - A. Consolidated Statements and Other Financial Information –Legal Proceedings”.

Further, predefined damages (set forth in the Consumer Protection Law) for a discrepancy from a customer's pricing plan, remedied after the customer complained, may aggregate to substantial amounts if paid to numerous customers on multiple occasions.

We employ thousands of employees and are therefore subject to the risk of employee lawsuits, including class action suits by employees.

We are subject to the risk of intellectual property rights claims against us, in relation to our products and services including TV service and other content related services, including video, photographs, music, music-related or other content we purchase from third party content providers. These claims may require us to initiate or defend protracted and costly litigation, regardless of the merits of these claims. If any of these claims succeed, we may be forced to pay damages or may be required to obtain licenses for the infringing product or service, which, if in substantial sums, could harm our results of operations. If we cannot obtain all necessary licenses on commercially reasonable terms, we may be forced to stop using or selling the products and services. We may not have insurance coverage for these types of claims.

Our operations are dependent on complex technology and information systems.

Our operations are dependent on a number of complex technological and information systems, including billing systems. The occurrence of malfunctions in such complex and ever changing and expanding systems is inevitable. In addition, we are in the process of implementing a unified customer relation management, or CRM, system for both our cellular and fixed-line operations, which may result in larger expenditures than anticipated, require significant management attention that would otherwise be available for our ongoing business, or lead to unforeseen operating difficulties and malfunctions. A malfunction in any of our systems which severely impacts our ability to provide products and services to our customers or adequately bill them, may result in loss of revenues to us, may adversely impact our brand and service perception, and expose us to legal claims and regulatory sanctions, all of which may adversely affect our results of operations.

Cyber attacks impacting our networks or systems could have an adverse effect on our business.

Cyber attacks, including through the use of malware, computer viruses, dedicated denial of services attacks, credential harvesting and other means for obtaining unauthorized access to or disrupting the operation of our networks and systems and those of our suppliers, vendors and other service providers, could have an adverse effect on our business. Cyber attacks may cause equipment failures, loss, disclosure, access, usage, corruption, destruction or the appropriation of information, including sensitive personal information of customers or employees, or valuable content and technical and marketing information, as well as disruptions to our or our customers' operations. Cyber attacks against companies, including Cellcom, have increased in frequency, scope and potential harm in recent years. Further, the perpetrators of cyber attacks are not restricted to particular groups or persons. These attacks may be committed by company employees and agents, advertently or inadvertently, or by external actors operating in any geography, including jurisdictions where law enforcement measures to address such attacks are unavailable or ineffective, and may even be launched by or at the behest of nation states. The preventive actions we take to reduce the risks associated with cyber attacks, including protection of our systems and networks, may be insufficient to repel or mitigate the effects of a major cyber attack in the future.

The inability to operate our networks and systems or those of our suppliers, vendors and other service providers as a result of cyber attacks, even for a limited period of time, may result in significant expenses to us and/or a loss of market share to other communications providers. The costs associated with a major cyber attack on us could include expensive incentives offered to existing customers and business partners to retain their business, increased expenditures on cybersecurity measures and the use of alternate resources, lost revenues from business interruption and litigation. The potential costs associated with these attacks could exceed the insurance coverage we maintain. Further, certain of our businesses, such as those offering security solutions and infrastructure and cloud services to business customers, could be negatively affected if our ability to protect our own networks and systems is called into question as a result of a cyber attack. In addition, a compromise of security or a theft or other compromise of valuable information, such as financial data and sensitive or private personal information, could result in lawsuits and government claims, investigations or proceedings. Any of these occurrences could damage our reputation and could further result in material adverse affect on our results of operation or financial condition.

There are certain restrictions in our licenses relating to the ownership of our shares.

Our cellular license restricts ownership of our ordinary shares and who can serve as our directors, as follows:

- our founding shareholder, Koor Industries Ltd. (wholly owned by DIC), or Koor (or its transferee or transferees, if approved in advance by the Ministry of Communications as "founding shareholders"), must own at least 26% of each of our means of control;

- Israeli citizens and residents among our founding shareholders (or their approved transferees) must own at least 5% of our outstanding share capital and each of our other means of control;

- a majority of our directors must be Israeli citizens and residents;

- at least 10% of our directors must be appointed by Israeli citizens and residents among our founding shareholders; and

- we are required to have a security committee of our Board of Directors that deals with matters relating to state security.

If these requirements are not complied with, we could be found to be in breach of our license and our license could be changed, suspended or revoked.

In addition, our license provides that, without the approval of the Ministry of Communications, no person may acquire or dispose of shares representing 10% or more of our outstanding share capital. Further, our directors and officers and any holder of ordinary shares representing 5% or more of our outstanding share capital may not own 5% or more of Bezeq or any of our competitors or serve as a director or officer of such a company, subject to certain exceptions, which require the prior approval of the Ministry of Communications.

To ensure that an unauthorized acquisition of our shares would not jeopardize our license, our articles of association provide that any shares acquired without approval required under our license will not be entitled to voting rights.

We may be adversely affected by the significant technological and other changes in the telecommunications industry.

The telecommunications market is known for rapid and significant technological changes and requires ongoing investments in advanced technologies in order to remain competitive. In recent years we have witnessed an immense growth of data traffic on both cellular and fixed-line networks which required us to upgrade our cellular and fixed-line networks and purchase increasingly large capacity for our fixed-line internet connectivity and infrastructure services to accommodate such demand. We estimate that data traffic will continue to rapidly grow in the future, among other things, due to high definition and 4K content and TV services provided over the internet (both cellular and landline). To meet the growing demand for cellular data traffic, we are required, among other things, to continue our investment in our 4G network and the upgrade of our transmission network to allow larger capacity and higher data speed rates. To meet the growing demand for landline data traffic and find more cost effective alternatives for the capacity we purchase from other landline operators who own a widespread landline broadband infrastructure, we have invested in deploying our own infrastructure and have entered into several agreements with IBC, including investment in IBC, indefeasible right of use, or IRU to IBC's infrastructure and sale to IBC of our independent fiber-optic infrastructure in residential areas (see also "Item 4. Information on the Company – B. Business Overview – Network and Infrastructure – Fixed-line Segment – Fixed-line Infrastructure – Investment in IBC"). Such endeavors are both costly and require management attention which could have been directed elsewhere.

Further, the Ministry of Communications determined that the replacement of our and another operator's 850 MHz frequencies with 900 MHz frequencies compatible with international standardization for our region will be effected no later than March 2021,and that our 850MHZ frequencies allocation will expire on February 1, 2022. Such replacement, if effected, will entail a complex and sensitive engineering project, involving material investments in our networks, including the replacement of radio equipment in all of our cellular sites and may, during such project, adversely affect our products and services and impose a material hardship on the Company, both financially and operationally. Further, some of the frequencies to which we may be required to transfer are not specifically detailed in the Plan, which may impose additional hardship on such replacement. See "We may not be able to obtain permits to construct and operate cell sites". We informed the MOC that such replacement requires a much longer period and requires the fulfilment of certain conditions precedent which have not been fulfilled to date. Execution of such a replacement within a shorter timeframe, such as the timeframe set by the MOC, will increase the negative effects detailed above.

In addition, in December 2018 the MOC published principles for a frequencies tender the MOC intends to conduct in Q4/2019. According to the MOC's announcement, the tender is to include 25MHz in the 700Mhz frequencies band, up to 10Mhz in the 800Mhz frequencies band, 60MHz in the 2600 MHz frequencies band and 300 MHz in the 3500-3,800Mhz frequencies band with maximum allocation of 15MHz per network in the 700MHz frequencies band. As the 700MHz would serve as the main coverage enhancement frequency for 5G services (the 800MHz frequencies band shall become available sometime in the future and the 3500-3800MHz frequencies are limited and cannot provide large coverage), the limited amount of 700MHz frequencies included in the tender and the maximum allocation per network, the tender may result in not all MNOs winning such frequencies or winning less frequencies than their competitors, which may lead to a bidding war and harm the ability to provide 5G services. A frequencies tender will require us to make additional investments in purchasing the frequencies and thereafter to make additional investments in our networks while we aim to decrease our expenses and investments. Participating in a frequencies tender and the said additional investments, more so if a bidding war will result in higher consideration for the frequencies, may have a substantial adverse effect on our results of operations. Further, failing to win 700MHz at all or in a smaller amount than our competitors, may have an adverse effect on our competitive standing and as a result, on our results of operations. See "Item 4. Information on the Company – B. Business Overview — Network and Infrastructure – Cellular Segment – Frequencies".

Given the current low profitability of our business, we may be forced to decrease investments in our business and specifically in our networks, such as in relation to future generations and technologies, and the aforementioned frequencies tender which may adversely affect our future services, competitiveness and future results of operations. See also "As a result of substantial and continuing changes in our regulatory and business environment, our operating results, profitability and cash flow have decreased significantly in the past several years, with a loss for 2018. Further declines may adversely affect our financial condition".

If we fail to compensate for increased expenses or investments (especially in comparison to our competitors, not all of which will be required to make similar investments or pay increased expenses), due to, among other things, the competitive environment, our results of operations may be materially adversely affected.

Our handsets revenues and profitability decreased further in 2018 and may continue to decrease.

Handsets sales account for a substantial portion of our revenues and profitability. In recent years additional competitors have entered the handset market and increased the competition in this market and less successful launches of handset models and increased sales of handsets in the Israeli VAT free city (Eilat) have contributed to the decrease in our revenues from handsets. Our end user equipment revenues in 2018 were NIS 655 million ($173 million), a decrease of 14.9% from NIS 770 million ($205 million) in 2017 and a decrease of 21.6% from NIS 836 million ($223 million) in 2016. Additional changes to this market, including the entry of additional competitors, including online retailers, both domestic and international, changes of distribution channels or customers purchasing habits, lack of successful launches of new less attractive handset models or any other reasons resulting in decreased sales by us or in general (for example, Apple, one of our major handsets vendor, has forecasted a slowdown in handsets sales), new legislation and decisions by regulators or the courts effecting our ability to market handsets or our profitability therefrom, may materially adversely affect our handset sales and profitability. See also "We face intense competition in all aspects of our business." above.

Our network sharing agreements consideration constitute a significant portion of our revenues

Under our network sharing agreement with Golan Telecom Ltd., or Golan, we are entitled to an average annual consideration of over NIS 200 million over the agreement term and under our network sharing agreement with Marathon 018 Xfone Ltd., or Xfone, we are entitled to the higher of a minimum annual consideration increasing over time or per user consideration (see "Item 4. Information on the Company – B. Business Overview — Network and Infrastructure – Cellular Segment – Network sharing agreements"(. Should Golan or Xfone fail to make full and timely payments to us, due to financial difficulties, disagreements with us, or otherwise, this could materially adversely affect our results of operation.

Our substantial debt increases our exposure to market risks, may limit our ability to incur additional debt that may be necessary to fund our operations and could adversely affect our financial stability

As of December 31, 2018, our total indebtedness and long-term loans were approximately NIS 3,865 million ($1,031 million), with our net debt at approximately NIS 2,263 million ($604 million). For additional details see "Item 5. Operating and Financial Review and Prospects. – B. Liquidity and Capital Resources – General". The terms of our debentures and other credit facilities currently permit us to incur additional indebtedness (subject in some cases to certain limitations). Our substantial debt could adversely affect our financial condition by, among other things:

- increasing our vulnerability to adverse economic, industry or business conditions, including increases in the Israeli Consumer Prices Index, or CPI, as approximately NIS 1,326 million ($354 million) is CPI linked;

- limiting our flexibility in planning for, or reacting to, changes in our industry and the economy in general;

- requiring us to dedicate a substantial portion of our cash flow from operations to service our debt, thus reducing the funds available for operations and future business development, as well as for dividend distribution; and

- limiting our ability to obtain, or resulting in less favorable terms and pricing for, additional financing to operate, develop and expand our business or for refinancing existing debt.

Israeli institutional investors must follow certain procedures and requirements before investing in non-governmental debentures. As a result, our series F and H through L indentures include certain limitations and covenants, including a covenant not to issue additional debentures if it involves a rating downgrade, certain financial covenants, negative pledge, cross default, limitation on the distribution of dividends, obligation to pay additional interest in case of certain rating downgrades (which occurred under our series F and G debentures in June 2013). For details regarding such limitations and covenants see "Item 5. Operating and Financial Review and Prospects. – B. Liquidity and Capital Resources – Debt Service". These limitations are expected to apply to any additional debt incurred by us. These procedures, limitations and covenants limit our freedom to conduct our business, may impose additional costs on us and may limit our ability to borrow additional debt from Israeli institutional investors as well as adversely affect the terms and price of such debt raising. Further, interest rates are currently very low and future increase of the interest may increase costs for future debt raising.

Any further downgrade in our rating, and any adverse change in our financial results, including any increase in our Net Leverage (defined in our series F and H through L indentures and other credit facilities as the ratio of net debt to EBITDA during a period of 12 consecutive months, excluding one-time events), may adversely affect the terms and price of debt raised, particularly through the issuance of debentures to institutional investors.

Under the Concentration Law, the Israeli Minister of Treasury must set limitations regarding the aggregate credit that may be provided by Israeli financial institutions to a corporation or a business group (defined as a controlling shareholder and the corporations under its control), which may adversely affect our ability to raise debt from Israeli financial institutions.

Under the “Guidelines for Sound Bank Administration” issued by the Israeli Supervisor of Banks, Israeli banks are subject to limitations on lending money to a single borrower and one group of borrowers and on the aggregate credit that may be provided to large borrowers and groups of borrowers. Under the relevant regulations, Israeli institutional investors are also subject to certain limitations on their total investments (including debt investments) in a single corporation and a group of corporations. This may limit our ability to obtain additional financing to operate, develop and expand our business or to refinance existing debt because, for such purposes, we are deemed to be included in the same group as DIC.

Our business results may be affected by currency fluctuations, by our currency hedging positions and by changes in the Israeli Consumer Price Index

A portion of our cash payments are incurred in, or linked to, foreign currencies, mainly U.S. dollars. In particular, in 2016, 2017 and 2018, payments denominated in, or linked to, foreign currencies, mainly U.S. dollars, represented approximately 14%, 16% and 17%, respectively, of our total cash outflow (including payments of principal and interest on our debentures). As almost all of our cash receipts are in NIS, any devaluation of the NIS against the foreign currencies in which we make payments, will increase the NIS cost of our foreign currency denominated or linked expenses and capital expenditures.

Furthermore, since the principal amount of and interest that we pay on our Series F, H and J debentures, are linked to the Israeli CPI, any increase in the Israeli CPI will increase our financing expenses and could adversely affect our results of operations.

We purchase derivative financial instruments in order to hedge part of the foreign currency risks and CPI risks deriving from our operations and indebtedness. Derivatives are initially recognized at fair value. Changes in the fair value of such derivatives are recognized through our income statement upon occurrence. These differences in the derivative instruments' designation could result in fluctuations in our reported net income on a quarterly basis.

We may not be able to fulfill our dividend policy in the future; implementation of our dividend policy will significantly reduce our future cash reserves.

Our dividend policy targets a payout ratio of at least 75% of our net income in each calendar year, subject to any applicable law, our license and contractual obligations and provided that such distribution would not be detrimental to our cash needs or to any plans approved by our Board of Directors. Our series F and H through L indentures and other credit facilities contain a covenant not to distribute more than 95% of the profits available for distribution according to the Israeli Companies Law, or Profits. Moreover, under such indentures and other credit facilities, if our Net Leverage exceeds 3.5:1, we may not distribute more than 85% of our Profits and if our net leverage exceeds 4.0:1, we may not distribute more than 70% of our Profits. For additional details see "Item 5. Operating and Financial Review and Prospects – B. Liquidity and Capital Resources – Debt Service". In addition, our license requires that we and our 10% or more shareholders maintain at least $200 million of combined shareholders’ equity. Dividend payments are not guaranteed and our Board of Directors may decide, in its absolute discretion, at any time and for any reason, not to pay dividends or to pay dividends at a ratio to net income that is less than that set in the policy. Since the fourth quarter of 2013, our board of directors chose not to declare dividends, given the intensified competition and its adverse effect on our results of operations and in order to strengthen our balance sheet. See “Item 8. Financial Information - A. Consolidated Statements and Other Financial Information - Dividend Policy”.

Our dividend policy, to the extent implemented, will significantly reduce our future cash reserves and may adversely affect our ability to fund unexpected capital expenditures. As a result, we may be required to borrow additional money or raise capital by issuing equity securities, which may not be possible on attractive terms or at all.

If we are unable to fulfill our dividend policy, or pay dividends at levels anticipated by investors in our shares, the market price of our shares may be negatively affected and the value of our investors’ investment may be reduced.

We rely on certain suppliers for key equipment and services. We do not own a widespread infrastructure in the landline market and are dependent on infrastructure providers.

We depend upon a small number of suppliers to provide us with key equipment and services. For example, Nokia Networks Israel, or NSN, provides our GSM/GPRS/EDGE/UMTS/HSPA/LTE core system, radio access network and related products and services and Carrier Ethernet network (previously provided by Alcatel Lucent Israel Ltd.); LM Ericsson Israel, or LM Ericsson, supplies part of our radio access network and related products and services based on UMTS/HSPA technology and our OTT TV services platform (recently sold); Cisco Systems, Inc., or Cisco, provides our SDH equipment for our transmission and ISP network; and Be'eri Printers provides our printing supplies and invoices as well as the distribution, packaging and delivery of invoices and other mail to the postal service distribution centers. In addition, we lease a small portion of our cellular related transmission capacity from Bezeq, the incumbent landline operator. Our OTT TV services are further dependent on the Israeli Second Radio and Television Authority, the authority responsible for linear channels of the digital terrestrial television (DTT) broadcasting in Israel.

We are further dependent on infrastructure providers for our internet connectivity, broadband infrastructure (using the landline wholesale market), International Long Distance calls, or ILD, landline telephony (using Voice over Broadband, or VOB, technology), and OTT TV services. Those providers include Bezeq and Hot, which provide broadband infrastructure in Israel, TI Sparkle Ireland Telecommunications Ltd. (formerly Mediterranean Nautilus Ltd.) and TI Sparkle (Israel) Ltd. (formerly Mediterranean Nautilus (Israel) Ltd.), or collectively TI Sparkle, which connects the Israeli internet network to the global internet network, as well as Israeli telephony, via an underwater communications cable. We are dependent on Bezeq for the provision of our wholesale broadband infrastructure services as well as for the deployment of our independent infrastructure using Bezeq's infrastructure. Should an effective telephony service be provided under the wholesale market and the wholesale market effectively apply to Hot as well, we would be dependent on them for such services as well (the wholesale market over Hot's infrastructure is in its early stages). Bezeq has breached certain regulatory obligations in the equal provision of wholesale services to its retail customers or refused to provide them at all, and has prevented and delayed the deployment of our independent infrastructure, including through labor disruptions by its employees, and such occurrences may adversely affect us in the future as well. See also "Item 4. Information on The Company – B. Business Overview – Fixed-line Segment".

In addition, our cellular end-user equipment sales have been dominated in recent years by Apple and Samsung products, representing over half of our handset sales. See "Item 4. Information on the Company – B. Business Overview – Cellular Segment – Handsets" for additional details.

Vubiquity Management Ltd., or VU, provides us international content and content operation services for our OTT TV services. RGE Group Ltd., or RGE, ONE Sport TV services Ltd., or ONE, and Charlton Ltd., or Charlton, each provides us with unique sports content. Keshet Broadcasting Ltd. and Reshet Media Ltd. provide us each with a linear channel and the right to include certain of such content in our VOD catalogue.

We rely on agreements with foreign carriers to provide cellular roaming capabilities to our cellular subscribers, ILD services to our cellular and landline subscribers, as well as international voice hubbing (providing ILD services to foreign operators) services. We cannot control or compel the improvement of the quality of the service that they provide and it may be inferior or less advanced than the service that we provide.

In general, if these suppliers fail or refuse to provide equipment, content or services to us that meet requisite quality standards or on a timely basis, at unfavorable terms to us or provide our competitors more favorable terms and conditions, or if these suppliers fail to produce successful and desirable products or content when no equivalent alternatives are available, or if such suppliers raise the pricing of their products or content (for example, TV sports content prices in Israel have substantially increased with the entry of additional competitors), or if a regulatory change prevents our OTT TV customers from using the DTT or condition such usage on unfavorable terms or degradation of service quality, we may be unable to provide services or products to our subscribers in an optimal manner until an alternative source, if one is available, can be found or the situation is rectified, which may harm our ability to compete and result in loss of customers and revenues or place our licenses at risk of revocation for failure to satisfy the required service standards and subject us to customers' lawsuits.

Our investment in new businesses involves many risks.

We have invested and expect to continue to invest in exploration and development of new business opportunities in order to extend and complete our capabilities and offerings, such as the investment in IBC or deployment of a wide-spread landline infrastructure, and our entrance into the Internet of things (IOT) field. In addition to substantial investments in IBC (if materializes) in order to comply with its deployment obligations, we would be obligated to purchase 10-15% of IBC’s fiber optics connected to buildings. Such endeavors may involve significant risks and uncertainties, including shift of management attention from our ongoing business, loss of focus of our sales and marketing efforts on our main businesses due to attention given to new businesses, insufficient revenues to offset liabilities assumed and expenses associated with these new investments, adversely affecting our cash flow, inadequate return of capital on our investments, regulatory changes which may impose additional burdens than planned, inability to effectively compete with incumbent providers or new competitors entering the market, and unidentified issues not discovered in our due diligence of such strategies and offerings, such as unforeseen implementation obstacles and large expenditures. Because these new ventures are inherently risky, no assurance can be given that such strategies and offerings will be successful and will not materially adversely affect our reputation, financial condition, and operating results. Moreover, entry into such new ventures may trigger increased competitive pressure by the incumbent providers of competing services on our core business, aiming at preventing our efforts to compete with them at the relevant market.

We are controlled by a single shareholder who can significantly influence matters requiring shareholders’ approval.

As of January 31, 2019, Koor held, directly and indirectly, approximately 44.08% of our outstanding share capital (including 5% of our share capital held through a lending transaction by Koor to two Israeli shareholders, which are considered joint controlling shareholders with Koor and who undertook, among others, to vote with Koor in all shareholders resolutions) and the voting rights in respect of an additional approximately 2.94% of our share capital, pursuant to shareholders agreements among Koor and certain of our minority shareholders. Accordingly, subject to legal limitations, Koor has control (as the term "control" is defined in the Israeli Securities Law, 1968, or the Israeli Securities Law, namely the ability to direct a company's activities) over all matters requiring shareholder approval, including the election and removal of our directors (other than external directors) and the approval of significant corporate transactions. This concentration of ownership could delay or prevent proxy contests, mergers, tender offers, open-market purchase programs or other purchases of our ordinary shares that might otherwise give our shareholders the opportunity to realize a premium over the then-prevailing market price for our ordinary shares.

Risks Relating to Operating in Israel

We conduct our operations in Israel and therefore our results may be adversely affected by political, economic and military instability in Israel.

Our operations, our network, our customers and some of our suppliers are located in Israel. Accordingly, political, economic and military conditions in Israel may directly affect our business. Any armed conflicts, terrorist activities or political instability in the region or hostilities involving Israel or the interruption or curtailment of trade within Israel or between Israel and its trading partners could adversely affect our operations, including due to a decrease in the number of tourists visiting Israel and increasing criticism of Israel in the international community (such as the increasing international pressure to boycott Israeli companies, including through the United Nations' Human Rights Council "name and shame list", especially when such companies operate in territories held by Israel in Judea and Samaria, as we and other Israeli operators are required to do under our license), and could make it more difficult for us to raise capital. Further, a substantial part of our network and information systems is located within range of missile strikes from the Gaza Strip and Lebanon. Any damage to our network or information systems may damage our ability to provide service, in whole or in part or otherwise damage our operation and could have an adverse effect on our business, financial condition or results of operations.

In addition, in the event that the State of Israel relinquishes control over certain territories currently held by it to the Palestinian Authority, we will not be able to provide service from our cell sites located in Israeli populated areas and on connecting roads in these territories. This may result in the loss of subscribers and revenues and in a decrease in our market share.

Our freedom and ability to conduct our operations may be limited during periods of national emergency.

Israeli law permits the Prime Minister of Israel, for reasons of state security or public welfare, to order a telecommunications license holder to provide services to or to establish a telecommunications facility for the security forces, and entitles the Israel Defense Forces to register or take engineering equipment and facilities as may be required for the security forces to carry out their duties. Israeli law also permits the Israeli Government, during national emergencies or for reasons of national security, to take all necessary actions in order to ensure state security, including taking control of our network. If national emergency situations arise in the future and if we are to be subject during such time to any of the foregoing actions, this could adversely affect our ability to operate our business and provide services during such national emergencies and adversely affect our business operations. Our other licenses contain similar restrictions.

Provisions of Israeli law and our license may delay, prevent or impede an acquisition of us, which could prevent a change of control.

The Companies Law regulates mergers, requires tender offers for acquisitions of shares above specified thresholds, requires special approvals for transactions involving directors, officers or significant shareholders and regulates other matters that may be relevant to these types of transactions. Further, the provisions of our licenses require the prior approval of the Ministry of Communications for changes of control in our Company.

Furthermore, Israeli tax considerations may make potential transactions unappealing to us or to our shareholders whose country of residence does not have a tax treaty with Israel exempting such shareholders from Israeli tax. With respect to mergers, Israeli tax law allows for tax deferral in certain circumstances but makes the deferral contingent on the fulfillment of numerous conditions, including a holding period of two years from the date of the transaction during which sales and dispositions of shares of the participating companies are restricted. Moreover, with respect to certain share swap transactions, the tax deferral is limited in time, and when the time expires, tax then becomes payable even if no actual disposition of the shares has occurred.

These provisions could delay, prevent or impede an acquisition of us, even if such an acquisition would be considered beneficial by some of our shareholders.

Risks Relating to Our Ordinary Shares

A substantial number of our ordinary shares could be sold into the public market, which could depress our share price.

Our largest shareholder, Koor, holds approximately 44.08% of our outstanding ordinary shares, as of January 31, 2019 (of which 5% are held (through a lending transaction) by two Israeli shareholders, which are considered joint controlling shareholders with Koor). The market price of our ordinary shares could decline as a result of future sales by Koor or other existing shareholders or the perception that these sales could occur. Sales may be made pursuant to a registration statement, filed with the U.S. Securities and Exchange Commission, or the SEC, pursuant to the terms of a registration rights agreement or otherwise, or in reliance on an exemption from the registration requirements of the Securities Act, including the exemptions provided by Rule 144. Any decline in our share price could also make it difficult for us to raise additional capital by selling shares.

In addition, pursuant to our capital offering effected in June 2018, we have issued 3,030,300 Series 2 options which may be exercised until June 24, 2019 . See "Item 5. Operating and Financial Review and Prospects. – B. Liquidity and Capital Resources – General".

In addition, under our 2015 option plan, options are subject to vesting schedules but vesting will be accelerated upon certain events including any sale or other disposition of all, or substantially all, of our outstanding shares. As of December 31, 2018 we had 780,332 shares reserved for issuance upon the exercise of options. See "Item 6. Directors, Senior Management and Employment – E. Share Ownership –Share Incentive Plans".

ITEM 4. INFORMATION ON THE COMPANY

A. HISTORY AND DEVELOPMENT OF THE COMPANY

Our History

Cellcom Israel Ltd. was incorporated in 1994 in Israel. Our principal executive offices are located at 10 Hagavish Street, Netanya 4250708, Israel and our telephone number is (972)-52-999-0052. Our authorized U.S. representative, Puglisi & Associates, is located at 850 Library Avenue, Suite 204 Newark, Delaware 19711 and our agent for service of process in the United States, CT Corporation System, is located at 111 Eighth Avenue, New York, NY 10011.

In February 2007 we listed our shares on the NYSE and in July 2007 we dual listed our shares on the Tel Aviv Stock Exchange, or TASE, and began applying the reporting leniencies afforded under the Israeli Securities Law to companies whose securities are listed both on the NYSE and the TASE.

As of January 31, 2019, Koor, wholly owned by DIC, currently directly and indirectly holds approximately 44.08% of our share capital (including through being joint controlling shareholder together with two Israeli shareholders of 5% of our outstanding share capital held by them through a lending transaction as of January 2018) and the voting rights in respect of an additional approximately 2.94% of our share capital.

As of the date of this Annual Report on Form 20-F, there has been no indication of any public takeover offer by any third party, in respect to our ordinary shares, or by us, with respect to another company’s shares.

In December 2014 and May 2015 we entered the TV and internet infrastructure markets, respectively, which completed our communications offering to include all communications services in Israel.

In 2017 we completed a reorganization of our subsidiaries, following which all our landline operations are unified under our wholly owned subsidiary Cellcom Fixed Line Communications, Limited Partnership.

In 2017, our network sharing and hosting agreements with Golan and Xfone, and a third agreement combining the 4G network arrangements in the previous two agreements into a three-way agreement (the Xfone agreement, Golan agreement and the three-way agreement shall be referred to as the Sharing Agreements) came into force. For details of our network sharing and hosting agreements with Golan and Xfone, see "B. Business Overview – Network and Infrastructure – Cellular Segment – Network sharing agreements" below.

In March 2019, we entered into a transaction for investment in IBC. "Item 4. Information on the Company – B. Business Overview – Network and Infrastructure – Fixed-line Segment – Fixed-line Infrastructure – Investment in IBC"

We hold a general license for the provision of cellular telephone services in Israel, granted by the Ministry of Communications in 1994 and valid until 2022. We also hold a unified general license for the provision of fixed-line services, granted by the MOC in 2015 and valid until 2026.

The SEC maintains an internet website that contains reports and other information about issuers, like us, that file electronically with the SEC. The address of that website is www.sec.gov. The Company's website address is www.cellcom.co.il. The information contained on, or that can be accessed through, the Company's website is not part of, and is not incorporated into, this Annual Report.

Principal Capital Expenditures

Our accrual capital expenditure in 2016, 2017 and 2018 amounted to NIS 382million, NIS 550 million and NIS 648 million, respectively. Accrual capital expenditure is defined as investment in fixed assets and intangible assets, such as investments in our communications networks, information systems, software and TV set-top boxes and capitalization of part of the customer acquisition costs as a result of the adoption of IFRS15.

B. BUSINESS OVERVIEW

General

We operate in two main segments, “Cellular” and “Fixed-line”. The cellular segment includes the cellular communications services, end user cellular equipment and supplemental services. The fixed-line segment includes landline and long distance telephony services, internet infrastructure and connectivity services, television services, transmission services end user fixed-line equipment and supplemental services.

Services and Products

Cellular Segment

General

We are the largest provider of cellular communications services in Israel based upon number of subscribers and estimated market share as of December 31, 2018. As of December 31, 2018, we provided cellular communications services to approximately 2.851 million subscribers in Israel with an estimated market share of 27%. We offer a broad range of cellular services through our 2G, 3G and 4G network. These services include basic cellular telephony services, text and multimedia messaging, advanced cellular content and data services and other value-added services. We also offer international roaming services, a wide selection of handsets from various leading global manufacturers and repair services on most handsets we offer. Not all services are supported by all handsets or by all of our networks.

We offer our cellular subscribers a variety of usage and sector pricing plans and bundles combining cellular services with other communications services our group offers, including quatro bundles (internet infrastructure service and connectivity, landline telephony, TV service and cellular services). We offer two methods of payment: post-paid and pre-paid . Post-paid services are offered to subscribers who are willing to pay for our services through banking and credit arrangements, such as credit cards and direct debits. Pre-paid services are offered to cellular subscribers who pay for our services prior to obtaining them, usually by purchasing our “Talkman” pre-paid cards or “virtual” Talkman cards. The majority of our sales are post-paid. Price erosion and the marketing of packages have resulted in a constant decline in our pre-paid subscriber base. In line with regulation, our pricing plans do not include a commitment to purchase our services for a predefined period, other than in large business agreements.

We provide Golan and Xfone national roaming services under our Sharing Agreements and we provide the Joint Corporations services as a subcontractor. See "-Networks and Infrastructure - Network sharing agreements" below.

Basic cellular services

Our principal cellular service is basic cellular telephony and data transfer, upload and download (in supporting handsets). Both are included in our packages price plans. In addition, we offer many other services with enhancements and additional features to our basic cellular telephony service, including voice mail, cellular fax, call waiting, call forwarding, caller identification and conference calling.

Data services can be used with handsets (in supporting models), cellular modems and tablets. We provide our customers with a variety of "internet data packages" for that purpose.

We also offer both an outbound roaming service to our subscribers when traveling outside of Israel and an inbound roaming service to visitors to Israel who can “roam” on our network. As of December 31, 2018, we had commercial roaming relationships with 553 operators in 180 countries based on the standard agreements of the GSM organization (an umbrella organization in which all the cellular operators operating with GSM technology are members). In addition, as of December 31, 2018, we had 3G roaming arrangements with 382 of these operators in 114 countries (part of them for 4G as well), enabling our 3G and 4G roamers to use data services in the respective countries and visiting roamers in Israel of these operators to use our 3G and 4G services, respectively.

Value-added services

In addition to basic cellular telephony and data services, we offer many value-added services, such as Short Message Services, or SMS, and Multimedia Messaging Services, or MMS, cloud backup, content services such as "Cellcom Volume" our music application and "Cellcom tv" application and other applications such as a cyber security application and a parents' application against bullying on the Internet. We offer those services that we believe are likely to be popular with subscribers and benefit our business. Some of the value-added services that we offer are available only to subscribers who have supporting handset models and some are offered only to business subscribers.

To our business subscribers we also offer multi SMS, M2M, "Double Net" services allowing combined usage of cellular and landline networks in order to ensure continuous service, work force management, vehicles management applications and IOT (internet of things) solutions such as "smart city" end-to-end cellular and fixed line solutions. We are constantly considering and evaluating the possibility of introducing additional products and services to our customers.

Handsets

We sell a wide selection of handsets (which for purposes of this report may include other types of communications end-user equipment, such as tablets) designed to meet individual preferences. Prices of handsets vary based on handset features and special promotions. We offer a variety of installment plans for handsets and discounts for short term installment plans, although in most cases, handsets are to be paid for in 36 monthly installments. We offer a variety of handsets from world-leading brands such as Samsung, Apple, Xiaomi, LG, Sony and Nokia. The vast majority of our handset sales in 2018 have been by Samsung and Apple. The handset models we sell offer Hebrew language displays in addition to English, Arabic and Russian (in most of the models). We are also required to provide cellular services to subscribers who did not purchase their handsets from us, provided that the handset model complies with the standards set by the Ministry of Communications. For details regarding end user equipment repair services see "Customer Care" below.

We also sell tablets, streamers and added value products to our customers, such as smart watches and home security cameras.

Fixed line Segment

Our main fixed line services include our internet infrastructure (for private customers based mostly on the landline wholesale market and increasingly on our independent fiber-optic infrastructure and for business customers based on our landline infrastructure) and connectivity services, OTT TV services, ILD services, landline telephony services and transmission services (for business customers). We also offer bundles of these services, including a triple offering (internet service including infrastructure and connectivity, landline telephony, TV service) and quatro offering (internet services, landline telephony, TV service and cellular services). We also offer landline transmission and data services to selected business customers and telecommunications operators (including transmission revenues from Golan according to the network sharing agreement as of April 2017), using our fiber-optic infrastructure and complementary microwave links, IP switchboard services and operation and management of business telecommunications systems. Additional services include cloud services and data protection products solutions based on products and services offered by us and by third party vendors and IOT solutions such as "smart city" end-to-end cellular and fixed line solutions.

Internet infrastructure and Connectivity

We are a major provider of internet connectivity services. Prior to the formation of the landline wholesale market, the Israeli internet market was characterized by a separation between the internet infrastructure providers (mainly Bezeq and Hot) and the internet connectivity service providers. Consequently, the internet customer was required to enter into a contractual arrangement with both types of these providers. The infrastructure provider is responsible for the connection of the customer from his computer or other device to the infrastructure provider's operator. The internet service provider is responsible for providing access to the customer from the infrastructure provider's operator, through its own operator, to the local and global internet network. As of May 2015, following the inception of the landline wholesale market, we (and other operators) provide end-to-end internet service (infrastructure and connectivity) using Bezeq's infrastructure and more recently, over our independent fiber-optic internet infrastructure with first steps towards using Hot's infrastructure as well. We sell internet infrastructure services bundled with internet connectivity, as well as with our other services. For details regarding the landline wholesale market see "Business Overview – Competition – Fixed-line Segment – Landline" and "Government Regulation – Fixed-line Segment – Landline".

As of December 31, 2018, we provide end-to-end internet service, to approximately 269,000 households.

In addition, we offer our internet subscribers value added services, such as data protection services to our private subscribers and connectivity integration solutions and global communications solutions to our business customers, including firewalls, anti-virus and anti-spam software, overseas internet connectivity services and server hosting services. In addition, we provide internet connectivity services that offer the ability to filter the content viewed by the internet users. We are constantly considering and evaluating the possibility of introducing additional products and services to our customers.

OTT TV services

As of December 2014, we offer OTT-TV services, branded 'Cellcom tv' mostly to private customers. Cellcom tv is an hybrid OTT-DTT TV service provided to the Israeli market. The service includes a set-top box that enables linear channels, including based on the Israeli digital terrestrial television (DTT) broadcasting, other commercial channels and Video on Demand library subscription (SVoD), music streaming service and additional advanced features such as cloud recording and VoD playlist channels, for a highly competitive price. Cellcom tv service can generally also be accessed by smartphones, tablets, Smart TV and additional TV services' equipment like Apple TV and Android TV devices (TV anywhere). Our VoD catalogue and linear channels offer international and local content from top content suppliers. As of December 31, 2018, we provide OTT TV services to approximately 219,000 households.

ILD services

We are one of the major players in the Israeli ILD market. Our principal service in the ILD market is the provision of outgoing and incoming telephone calls with substantially worldwide coverage. We provide these services mostly to post-paid customers, but also to pre-paid customers mainly through the sale of calling cards. Most of the customers of the pre-paid services are foreign workers who reside in Israel.

In addition, we provide "Hubbing" services to non-Israeli international operators. Hubbing services are bridging services between two non-Israeli international operators. Such services are provided by us where there is no direct connection between two non-Israeli international operators or where pricing differences in different locations make such bridging service desirable.

Landline telephony services

We offer advanced, voice and data landline services to selected business customers. We also offer basic landline telephony services to private customers by VOB technology. Landline telephony service enables an end user to conduct a telephone conversation with another end user who uses either another landline or a cellular telephone or computer, either in Israel or overseas.

We estimate that our current market share in the Israeli landline telephony market is not material.

Internet of Things

IOT solutions provide the ability to connect various devices to the internet. We, together with strategic partners, offer IOT solutions based on a variety of communications solutions, including landline (WiFi) and cellular. We offer smart city solutions which include a central management and control system to manage the various solutions, water and electricity meter readout from a-far, smart parking, smart and efficient street lighting, smart cameras which include analytic capabilities for security solutions, smart sensors for efficient waste disposal, various environmental factors and flood alert, stress buttons for educational institutions as well as WiFi and broadband communication capabilities in public areas.

Networks and Infrastructure

Cellular Segment

General

We have built an extensive, durable and advanced cellular network system, enabling us to offer high-quality services to substantially the entire Israeli populated territory, while using a cost-effective design, utilizing shared components for our networks, where applicable. We seek to satisfy quality standards that are important to our subscribers, such as high voice quality, high data throughput rate, low "blocked call" rate (average rate of call attempts that fail due to insufficient network resources), low "dropped call" rate (average rate of calls that are terminated not in the ordinary course) and deep indoor coverage. Therefore, we have made substantial capital expenditures and expect to continue to be required to make substantial capital expenditures on our network system, though, pursuant to our Sharing Agreements, radio capital expenditures for the shared networks will be divided among the sharing parties.

Cellular Infrastructure

Our cellular network has developed over the years since we commenced our operations in 1994.

Our "fourth generation" LTE, or Long Term Evolution technology, was launched in August 2014, offers data throughput of up to 150 Mbps on the downlink path and up to 50 Mbps on the uplink path (voice services are provided through our 3G network). Our LTE network covers most of the population of Israel and in 2019 we intend to continue the deployment of this network in order to enable higher data throughput rate. The average throughput indicator is not set in our license. Our 4G network is shared with Golan and Xfone and operates in Multi Operation Core Network, or MOCN, mode.

Our "third generation" UMTS/HSPA+, or high-speed packet data access, technology, offers full interactive multimedia capabilities with current data rates of up to 42 Mbps on the downlink path and up to 5 Mbps on the uplink path. In 2019 we intend to continue to support the increasing demand for data traffic, while maintaining its quality of services. This network, considered to be a "3.9" technology, uses the same core as our GSM/GPRS/EDGE network and covers substantially all of the populated territory in Israel. Moreover, our UMTS/HSPA+ network supports types of services that require higher throughput and lower delay, such as video conferencing, and provides an adequate fallback for our LTE network by means of smart features and network load sharing. Our 3G network is shared with Golan and operates in MOCN mode.

Our "second generation" GSM/GPRS/EDGE 1800MHz network allows for voice calls, data transmission and multimedia services, although at slower speeds than our LTE and UMTS/HSPA+ networks, and covers substantially all of the populated territory in Israel. Our GSM/GPRS/EDGE technology is an advanced second-generation technology and considered to be a "2.75G" technology. It enables us to deliver multimedia and services at speed rates that are higher than the rates offered through regular "second generation" digital cellular technology. Packet data rates vary from 50 Kbps to 200 Kbps, depending mainly on handset capabilities. In addition, in the case of coverage gaps and for voice services supported by our GSM/GPRS/EDGE technology, the network provides a partial voice fallback for our LTE and UMTS networks.

Most of our traffic uses the UMTS/HSPA+ network with a continuous growth of data using our LTE network.

Our primary objective going forward is to continue deploying our LTE network and to continue to support the increasing demand for data traffic of our high speed UMTS/HSPA+ network and to continue to perform extensive optimization work to provide our subscribers with maximum capability to support video and other broad-bandwidth content. See "Item 3. Risk Factors – We may be adversely affected by significant technological and other changes in the telecommunications industry".

We provide connectivity for our cellular network mainly through our independent transmission network (based on our fiber-optic network and complementary microwave infrastructure), in substantially all of the populated territory of Israel. We lease complementary capacity from Bezeq. For additional details regarding our transmission network see "- Fixed-line segment – Fixed-line Infrastructure" below.

Pursuant to the requirements of all telephony service providers in Israel, our cellular network is interconnected, either directly or indirectly, to the networks of all other telephony service providers in Israel. Our network monitoring system provides around-the-clock surveillance of our entire network. The network operations center is equipped with sophisticated systems that constantly monitor the status of all switches and cell sites, identify failures and dispatch technicians to resolve problems. Operations support systems are utilized to monitor system quality and identify devices that fail to meet performance thresholds. These same platforms generate statistics on system performance such as dropped calls, blocked calls and handoff failures. Our network operations center is located in our Netanya headquarters. In addition, we have a duplicate back-up center in a separate location and a disaster recovery plan, or DRP, for all our engineering systems. The DRP also provides our network with additional advantages, including increased capacity in some cases and also provides us better durability and resilience. We also adopted a business continuity plan and a disaster recovery plan to ensure our ability to continue our operation in emergency situations in accordance with our license.

Spectrum allocation

Spectrum availability in Israel is limited and is allocated by the Ministry of Communications through a licensing process. We have been allocated 2 X 20 MHz in the 850 MHz frequency band previously used by our TDMA network and currently by our UMTS/HSPA base stations, 2 X 20 MHz in the 1800 MHz frequency band, 5 - 15 MHz (varying dependent on usage required in different areas), which are used by our LTE network and our GSM/GPRS/EDGE network (varying dependent on usage required in different areas) and 2 X10 MHz in the 2100 MHz frequency band used by our UMTS/HSPA network. We believe that our available spectrum is sufficient for our current needs.

Out of the 20 1800 MHz, 3MHz were allocated to us in August 2015 by the Ministry of Communications for 4G technologies (such as LTE, LTE Advanced). Unlike our other frequencies allocated to us for the duration of our license, these frequencies were awarded to us for a period of 10 years only.

The shared networks further use additional 2X10 MHz in the 1800 MHz frequency band. See "– Network sharing agreements" for additional details.

We pay frequency fees to the State of Israel.

The MOC has informed us that it has received an instruction from the International Telecommunications Union to commence a process to accord the frequencies used by Israeli cellular operators with European standards. As a result, we and another cellular operator that use some frequencies according to American standards, were required by the MOC to migrate to 900 MHz frequencies compatible with international standardization for our region no later than March 22, 2021, replacing our 850MHZ frequencies allocation which shall expire on February 1, 2022. The MOC has yet to provide the method and schedule in which such replacement will be executed, including interim frequencies allocations as required. The MOC noted that we may use an interim leniency to the Planning and Building Law, allowing, under certain conditions, replacement of cell sites without obtaining a building permit. Such frequencies replacement will entail a complex and sensitive engineering project, involving material investments and replacement of radio equipment in all our cellular sites and may, during such project, adversely affect our products and services or quality thereof. See "Item 3. Key Information – D. Risk Factors – We operate in a heavily regulated industry, which can harm our results of operations. Regulation in Israel has materially adversely affected our results", "-We may not be able to obtain permits to construct and operate cell sites" and "- We may be adversely affected by significant technological and other changes in the telecommunications industry".

In addition, in December 2018 the MOC published principles for a frequencies tender the MOC intends to conduct in Q4/2019. The MOC expects to publish the tender itself for a public hearing in Q2/2019. As per the MOC's announcement, the tender is to include 25MHz in the 700Mhz frequencies band, up to 10Mhz in the 800Mhz frequencies band, 60MHz in the 2600MHz frequencies band and 300 MHz in the 3500-3800Mhz frequencies band. The tender will be open for MNOs only, other than 100Mhz in the 3500MHz frequencies band which will be open for any contender. MNO which shall not win 3500-3800 frequencies shall not be able to provide 5G services. MNOs sharing a network shall provide a joint bid (subject to the MOC's prior approval) and maximum allocation of frequencies will be as follows: in the 700MHz frequencies band - 15MHz per network; in the 2600MHz frequencies band - 40MHZ per network; in the 3500-3800MHz frequencies band - 80MHZ per MNO and 120MHZ per network. The result being that at present the 700MHz would be the main coverage enhancement frequency for 5G services (the 800MHz frequencies band becoming available sometime in the future and the 3500-3800MHz frequencies are limited and cannot provide large coverage), but given the amount available and maximum amount per network, not all MNOs may win 700MHz frequencies or may win less frequencies than their competitors. See "Item 3. Key Information – D. Risk Factors – - We may be adversely affected by significant technological and other changes in the telecommunications industry".

Cell site construction and licensing

We construct cell sites based on our strategy to expand the geographical coverage and improve the quality of our network and as necessary to replace cell sites that need to be removed. Our acquisition teams survey the area in order to identify the optimal location for the construction of a cell site. In urban areas, this would normally be building rooftops. In rural areas, masts are usually constructed. Our transmission teams also identify the best means of connecting the base station to our network, based on our independent transmission network, either by physical optical fiber, microwave link or Bezeq landlines. Once a preferred site has been identified and the exact equipment configuration for that site decided, we begin the process of obtaining all necessary consents and permits. The construction of cell sites requires building permits from local or regional authorities, or an applicable exemption, as well as a number of additional permits from governmental and regulatory authorities, such as construction and operating permits from the Ministry of Environmental Protection in all cases, permits from the Civil Aviation Authority in most cases and permits from the Israeli Defense Forces in some cases. In special circumstances, additional licenses are required. See "Item 4. Information on the Company – B. Business Overview – Government Regulations – Cellular Segment – Permits for Cell Site Construction."

Network sharing agreements

In March and April 2017 our Sharing Agreements came into effect – (1) the 4G network sharing and 2G and 3G hosting services agreement with Xfone (which commenced operating in the cellular market in April 2018), (2) the 3G and 4G network sharing and 2G hosting services agreement with Golan (originally entered into with Electra and adopted by Golan, after being acquired by Electra) and (3) an agreement combining the 4G network sharing arrangements of the Xfone agreement and the Golan agreement into one three-way agreement.

The Sharing Agreements set the terms under which the sharing networks operate, including:

- Usage of the parties' relevant frequencies, management and operation by separate entities, or the Joint Corporations, possession of equal parts of the shared network active elements, investment in equal parts in future active elements and IRU of each sharing party to the other sharing parties and IRU by us to the other sharing parties and the Joint Corporations to our passive elements of the shared networks, services provided by us to the Joint Corporations, as a subcontractor and certain arrangements for separation of the parities and adding another sharing party.

- The agreements are for a term of ten years, and will be extended for additional periods, unless either party notifies otherwise. The termination of the Golan Agreement prior to the lapse of the first 10 years due to a breach by Golan will entitle us to liquidated damages of NIS 600 million plus VAT. In addition to standard termination causes, Xfone may terminate its agreement by prior written notice if it decides to cease operating in the cellular market in Israel.

- The average annual consideration to be received by us under the Golan agreement (starting with lower annual payments and increasing over the term) is expected to be in a range of approximately NIS 210-220 million plus VAT, depending on Golan's number of subscribers and their usage of the shared network and our 2G network.

The consideration for us under the Xfone agreement includes substantially similar arrangements (mutatis mutandis to its sharing and hosting agreement), but during a period of up to five years beginning April 2018, Xfone will be entitled to replace its payments for IRU to the passive network and operating costs with a monthly payment per subscriber, but in any case not less than certain minimum annual amounts (ranging between approximately NIS 20 million in the first year and approximately NIS 110 million in the fifth year).

Under the Golan Agreement (which replaces the former national roaming services agreement), in April 2017, we provided a loan to Golan in the sum of NIS 130 million for a period of 10 years.

Fixed-line Segment

Fixed-line infrastructure

We launched our SDH transmission network in 1999 and our Carrier Ethernet network in 2010. In 2015 we launched an MBH network intended to support all our cellular traffic. These networks cover the central populated areas in Israel and business parks. These networks enable us to provide our business customers with telephony and high speed and high quality transmission and data services and provides us with our own wireline connectivity / backhaul services for our cellular networks while reducing our need to lease capacity from Bezeq, the incumbent landline operator in Israel.

Our optical transmission network is strategically deployed in order to cover the major portion of Israel’s business parks from Nahariya in the north to Beer Sheva in the south and Afula and Jerusalem in the east, consisting of approximately 1,980 kilometers. The fiber-optic network is monitored by a fault-management system that performs real-time monitoring in order to enable us to provide high quality service. In order to efficiently complete our transmission network’s coverage to the majority of our cell sites and business landline and transmission subscribers, we use a microwave network as a complementary solution in those areas that are not served by our fiber-optic network. As of December 31, 2018, we had approximately 2,808 microwave links to both our cell sites and our landline and transmission subscribers.

Additional transmission capacity required for our fixed line services to business customers is leased from Bezeq and Hot.

We pay frequency fees for frequencies used by our microwave network to the State of Israel.

In 2017, in light of the growing demand for data capacity by our fixed-line subscribers, mainly in the private sector, which we purchased from Bezeq, we commenced expanding our fiber-optic network into residential areas, using certain physical infrastructure of Bezeq and in 2018 we continued deploying our independent fiber-optic infrastructure in residential areas. In addition, in March 2019, we entered into agreements for the investment in IBC, the purchase of an indefeasible right of use in IBC's fiber-optic network and a term sheet for the sale of our independent fiber-optic infrastructure in residential areas to IBC. See "- Investment in IBC" below. Deployment of independent fiber-optic infrastructure or through our investment in IBC, will require material investments. It may, however, allow us to reduce investments in independent fiber-optic infrastructure and reduce our costs and our dependency on Bezeq and Hot and may improve our ability to provide quality services and compete in the fixed-line services market. There is no assurance that the requisite regulatory approvals for our investment in IBC will be received and the agreement will be implemented, or even if implemented, will have the expected benefits.

In 2018, we continued to expand our Carrier Ethernet network and our ISP network backbone in Israel and abroad in order to support growing demand for capacity, upgraded the capabilities and capacity of our customer Quality of Experience systems and upgraded and improved the capabilities of our central system for the protection of our network against cyber attacks.

Our internet infrastructure is currently comprised of connectivity sites in two locations in Israel (Haifa and Petah-Tikvah), which provide our customers, through overseas connectivity points in London and Frankfurt, with connectivity to the global internet network. This internet infrastructure contains backup capability in order to ensure continuity of service.

Investment in IBC

In March 2019 we entered into the following definitive agreements, or the Transaction, which in addition to standard and customary conditions, include the following:

- Purchaser Agreements - We and the Israel Infrastructure Fund, or IIF, entered into partnership agreements for the purchase of 70% of IBC's share capital by a jointly and equally owned limited partnership (to be formed), or the Purchaser. The Purchaser Agreements contain an undertaking for an additional investment of up to NIS 200 million by both the Company and IIF, pro rata to their holdings in the Purchaser, over a period of 3 years and certain arrangements regarding a party's failure to make its share of the committed investment and regarding dead lock situations.

- Share Purchase Agreement, or SPA - The Purchaser, IBC, the Israeli Electric Company, or IEC and the other shareholders and main creditors of IBC entered an agreement for the purchase of 70% of IBC's share capital, through investment of the Purchaser in IBC, for a total amount of NIS 103.5 million (subject to certain consideration adjustment mechanism, with respect to IBC’s net working capital at closing), or the "Consideration, to be provided partly as investment and partly as shareholders' loan. The other 30% of IBC's issued and outstanding share capital will be owned by IEC. The Consideration shall be used to settle generally all of IBC's debts (other than a certain amount to IEC). The SPA contains certain precedent conditions to the closing of the transaction, including regulatory approvals, the receipt of updated licenses with reduced deployment obligations, as well as the effectiveness of the other agreements.

- Shareholders Agreement - The Purchaser and IEC (holding 70% and 30% of IBC's share capital, respectively) entered into a shareholders agreement. The agreement regulates the management of IBC, including certain arrangements regarding funding of IBC and dilution (and anti-dilution in certain circumstances) of non-participating shareholders.

- IRU Agreement – We and IBC entered into an agreement granting us an indefeasible right of Use, or IRU to a 10-15% percentage of IBC's fiber optics 'home pass' (i.e. fiber-optic actually reaching / connected to the building), as shall be deployed by IBC in the next 15 years (and may be extended to additional periods with no additional consideration other than annual maintenance payments). The undertaking is subject to certain conditions which should be satisfied at the closing of the SPA and certain amount is available immediately. The IRU consideration is subject to actual IBC's 'home pass' deployment, and is expected to increase each quarter based on the actual addition of 'home passes' deployed during such quarter and shall be paid in 40 quarterly installations (10 years), in addition to annual maintenance payments.

- IEC Services Agreement - IBC and IEC entered into an agreement updating IBC's existing right of use and services agreement for IBC's fiber-optic network when deployed over IEC's infrastructure. The IEC Services Agreement includes improved pricing and arrangements for IBC's exclusive right to deploy its fiber-optics over the IEC's electricity network and other services provided by IEC to IBC in relation thereof.

The Shareholders Agreement and the IEC Services Agreement shall become effective at, and are subject to, the completion of the SPA. The Purchaser Agreements and the IRU Agreement became effective upon signing.

The completion of the Transaction is not expected to have a material effect on our Company's results of operations. The execution of the Transaction will be subject to the said conditions precedent, including regulatory approvals. IBC has already filed a request with the Ministry of Communications for an updated license with reduced deployment obligations. There is no assurance that the Transaction will be approved and executed, nor as to its timing and terms. In addition, there is no assurance whether we will be able to gain the expected results from the implementation of these transactions.

Term Sheet for the sale of Residential fiber-optic

In addition, we and IIF entered a term sheet for the sale of our independent fiber-optic infrastructure in residential areas as shall be at the end of 2019, to IBC, for the sum of NIS180-200 million (subject to the rate of the fiber-optic deployment and the number of actual 'home pass' connected at the end of 2019 and certain adjustments). The consideration for the sale is expected to be partly financed by IBC's shareholders' loans, including by us. The Fiber-optic sale TS is not part of the Transaction. Once the sale is completed, the IRU Agreement, including our obligation to purchase percentage of IBC's fiber optics 'home pass' (as detailed above), shall apply to the infrastructure purchased from us (the combined amount of fiber-optic deployed at street level, is expected to surpass 400,000 potential customers, at the end of 2019). The transaction is conditioned on the parties entering a definitive agreement, further agreement with the IEC, closing of the SPA and regulatory approvals. There is no assurance that the parties will reach a definitive agreement, that the sale will be approved and executed, nor as to its timing and terms.

For additional details see "Item 3. Key Information – D. Risk factors – Risks related to our business - We face intense competition in all aspects of our business", "- Our investment in new businesses involves many risks" and "Item 4. Information on the Company –B. Business Overview – Competition – Fixed-Line Segment- Fixed-Line Infrastructure".

Suppliers

In April 2014, we entered into a framework agreement with NSN Israel, of Nokia Networks group, a worldwide leading network manufacturer, for the purchase of an LTE network, which also supports LTE Advanced technology (4.5 generation) and related services. This agreement also governs the purchase and services provided under our previous agreement with NSN, in relation to our GSM/GPRS/EDGE /UMTS /HSPA core system, radio access network and related products and services. We have an option to purchase maintenance services on an annual basis until March 2030.

In September 2005, we entered into an agreement with LM Ericsson for the purchase of UMTS radio access network and ancillary products and services and in December 2011 for the purchase of upgraded UMTS /HSPA products and related services. We have an option to purchase additional maintenance services on an annual basis until 2026.

We use Telcordia's (which was acquired by Ericsson) intelligent platform, or IN, which provides services to our networks and allows us, at minimal cost, to internally develop sophisticated services with a short time-to-market that are customized to local market requirements.

In addition, we have agreements with several Israeli engineering companies for the construction of our cell sites. We also purchase certain network components from other suppliers.

Samsung International Co. Ltd. provides us Samsung handsets and spare parts for such products, under terms, including price of products, agreed between us and Samsung from time to time.

In October 2016, we entered into an agreement with Apple Sales International for the purchase and distribution of iPhone handsets in Israel. Under the terms of the agreement, we have committed to purchase a minimum quantity of iPhone products over a period of three years, which are expected to represent a significant portion of our total cellular handsets purchase amounts over that period.

We have entered into a number of agreements with TI Sparkle between 2003 and 2019 for the purchase of rights of use of certain telecommunications capacities on TI Sparkle's underwater communications cables, which connect the Israeli internet network to the "entry points" of the global internet, as well as maintenance and operation services relating to these cables. Over the last few years we have increased the capacity purchased for significantly lower prices, as well as reduced maintenance costs. The term of the agreement with respect to capacity purchased from TI Sparkle is in effect until May 2032. We have the option to terminate agreements with respect to parts of the capacity in 2027.

We have also entered into agreements with Bezeq and Hot, the primary internet infrastructure providers in the Israeli market, for the provision of our connectivity services. Due to the increase in customer demand for broadband width in recent years, we are required from time to time to increase the capacity we purchase from Bezeq and Hot. The terms of the wholesale landline infrastructure service we purchase from Bezeq and Hot are mainly set in the landline wholesale market regulation. For additional details see "Government Regulation – Fixed-line Segment – Wholesale landline market".

In November 2009, we entered into an agreement with Alcatel Lucent for the purchase of our Carrier Ethernet network. We have an option to purchase maintenance services until 2022.

Under our agreement with Alcatel Lucent, we purchased an SDH transmission network. We purchase maintenance services for the network on an annual basis.

In February 2015, we entered into an agreement with Bynat Communications Computers Ltd., or Bynat, for the purchase and maintenance of an MBH transmission network by Cisco. In the agreement we agreed to purchase maintenance services for a term of 5 years from final acceptance (until 2019), and we may stop purchasing such services subject to the provision of a prior written notice. Thereafter we have an option to purchase maintenance services for a term of 8 years (until 2027).

In June 2004, we entered into an agreement with Nortel Networks Israel (Sales and Marketing) Ltd., or Nortel, , for the provision of our international communications switch, on which we base our ability to provide international calling service, as well as related equipment and services. From 2010, Geneband Inc. (which acquired Nortel's relevant business) provides us with support and maintenance services for the equipment provided under this agreement.

We have entered into an agreement with ECI Telecom Ltd. for the provision of transmission switches by ECI Telecom among our various location sites in Israel and overseas, used for our internet connectivity and ILD operations.

Our system for the provision of advanced centrex services based on cloud solutions to our business landline customers, is supplied by Broadsoft Ltd.

Our principal suppliers in the ILD market are Bezeq, Hot and the Israeli cellular operators. We have entered into interconnect agreements with them for facilitating inbound and outbound international traffic to and from their networks, as well as for billing and collection services for our services, for certain customers. We have also entered into agreements with more than 100 foreign carriers. These agreements regulate and facilitate our ILD services, as well as our international voice hubbing services.

In 2011, we entered into an agreement with LM Ericsson, for the purchase of our OTT TV services system and ancillary products and services. In 2018, LM Ericsson's media operations were purchased by MK Systems USA Inc., and MK Systems' Israeli subsidiary which continue to provide us with maintenance services for our system. We are currently negotiating a new maintenance agreement. Our OTT TV service also uses the Israeli DTT infrastructure. The DTT infrastructure may be used freely by our customers.

In 2013, we entered into an agreement with VU (recently purchased by Amdocs (Israel) Limited), a leading international supplier of multiplatform video services and solutions, for the supply of international video content and content operation and management services for our OTT TV service. Under our agreement with VU, we have committed to pay certain fixed amounts for such content and services. The Agreement is valid until the end of 2020; thereafter, it is renewable for additional periods of one year each, unless terminated by either party, subject to prior notice.

In October 2015, January 2016 and December 2016, we entered into agreements with RGE, ONE and Charlton, respectively, for the provision of sport channels, in which each of these suppliers holds exclusive broadcasting privileges. Each of the agreements is for a period of 5 to 6 years, during which time we are committed to pay each supplier certain minimum amounts.

We maintain a variety of information systems that enable us to deliver superior customer service while enhancing our internal processes.

Our billing and CRM systems are supported mostly internally. We also use a customer care system provided by PeopleSoft and supported mostly internally, inventory and suppliers management systems by Priority/Eshbel and SAP, a financial system by Coda and infrastructure integrations systems by Microsoft BizTalk and Oracle OSB.

In May 2016, we entered into several agreements aiming to provide us with a comprehensive CRM SAAS solution, on a cloud 'software as a service', or SAAS, basis, which, when completed, will gradually replace all our current CRM systems with one CRM solution. These agreements include the following main agreements:

An agreement with salesforce.com EMEA Limited, or Salesforce, for the provision of Salesfoce's CRM SAAS platform, including various products and services and support for the agreement term. The agreement is valid until August 2019. We also have an option to renew the agreement for two additional periods of 5 years each under certain terms.

Two agreements with Vlocity UK Ltd., or Vlocity, as follows: (i) an agreement for the provision of Vlocity's telecom-CRM SAAS solution, based on Salesforce platform, including support for such services for the agreement term. This agreement is valid until November 2019and (ii) an agreement for the development and customization for Salesforce's and Vlocity's CRM solution. This agreement will be valid until the project is completed, and may be terminated by us subject to prior written notice.

We use Nortel's CTI system for the management of incoming calls to our telephonic call centers.

We also use a knowledge management system relating to our various services and products by Aman, branded "Cellcopedia".

We use ERP solutions provided by SAP. We use a data warehouse based on an Oracle database system and various data mining tools, ETL by Informatica and reports generated by Cognos. The data warehouse contains data on our subscribers' usage and allows for various analytical segmentation of the data.

Cisco provides us maintenance proactive malfunction detection and consultant services for our IP networks equipment. The agreement is effective until the end of 2019.

We entered into an agreement with Be'eri Printers for our printing supplies and invoices as well as the distribution, packaging and delivery of invoices and other mail to the postal service distribution centers in 2003. The agreement is effective until the end of 2022.

Sales and Customer Care and Marketing

Sales and customer care

As part of our strategy to fully penetrate every part of the Israeli market, we combine our sales and customer care efforts in order to maximize sales opportunities and achieve cost efficiency alongside accessible and quality customer service. Our customer service unit is our main channel for preserving the long-term relationship with our subscribers and we focus on customer retention through the provision of quality service and customer care. In addition, subscribers are encouraged to subscribe to additional value-added and content services as well other communications services, in order to enhance customer satisfaction and increase revenues, with a specific focus on bundles of services. We offer pricing plans, value-added services, handsets, accessories and related services through a broad network of direct and indirect sales personnel. We design pricing plans and promotional campaigns aimed at attracting new subscribers and enhancing our ability to retain our existing subscribers. In order to achieve this goal, we systematically monitor and analyze our subscribers' preferences, characteristics and trends.

We pay our independent dealers commissions on sales, while our direct, employee sales personnel receive base salaries plus performance-based incentives. All of our, and our dealers', sales, customer care representatives and other customer-facing staff go through extensive training prior to commencing their work and thereafter regularly undergo training, and review of their performance in order to assure the quality of our services and to identify areas where we can improve.

We provide our customer facing representatives with a continually updated database, thus shortening the interaction time required to satisfy the customer’s needs and preventing human errors. We constantly review our performance by reviewing customers applications and conducting surveys among our subscribers in order to ensure their satisfaction with our services and to improve them as necessary. In addition, we constantly apply preventive and preemptive measures aimed at reducing churn.

In our efforts to adjust our costs to market conditions, we have closed or unified points of sale and service in neighboring locations and reduced or relocated call centers, operating them in a more cost effective fashion, while placing greater focus on self-service channels and proactive malfunction resolution, identifying and solving problems ahead of customer complaint.

Our sales and customer care operation is conducted primarily through the following channels:

Points of sale/Walk-in centers. We distribute our products and services through a broad network of physical points of sale providing us with nationwide coverage of our existing and potential subscriber base.

As of December 31, 2018, we independently operated approximately 22 service and sales centers, with approximately 200 additional sale and service points operated by our dealers (including our wholly owned dealer, Dynamica), covering almost all the populated areas of Israel. These centers generally offer the entire spectrum of products and services that we provide to our subscribers and potential subscribers. These stores are mostly located in central and other frequently visited locations to provide our subscribers with easy and convenient access to our products and services. In our efforts to penetrate certain sectors of our potential subscriber base, we select dealers with proven expertise in marketing to such sectors. Our walk-in centers also offer handset repair service or serve as a contact point for depositing the handsets for repair and receiving the repaired handset (in the same center or at a location of their choice by a courier), with the repair services conducted in a central lab.

In 2018, we continued reducing the space of several additional points of sale, and we may continue to do so in 2019.

Telephonic sales/Call centers. Telephonic sales efforts target existing and potential subscribers. Our sales representatives (both in-house and outsourced) offer our customers a variety of products and services, both in proactive and reactive interactions. Our call-center services are divided into several sub-centers: general services; technical services; billing; sales; international roaming; and data, internet and TV. We are constantly reviewing the effectiveness of our service and also operate a multi-function call center providing all our services. We currently operate call centers in nine locations throughout Israel, five of which are outsourced. In 2018, we witnessed an additional decrease in calls to our calls centers. During peak hours our call centers have the capability to respond to 600 customer calls simultaneously. We are making efforts to reduce the number of calls to our call centers by using our new CRM system to provide a more complete service and promoting our self-service channels.

Account managers. Our direct sales force for our business customers maintains regular contact with our mid-sized and large accounts. We provide small and mid-sized business customers one focal point to both sales and services by phone. Our account managers are aided by our various back office experts in determining customers' needs and making suitable offers, including tailor-made solutions, when required. We offer our business customers handsets repair services by a dispatch service. Sales to larger business customers or governmental and local authorities sometimes involve participation in the customer's tender process.

Online sales/Self service. We offer our customers the ability to purchase our products and services and receive various information through our internet site (and our OTT TV service dedicated internet site) and our smartphone application. We provide our subscribers and potential subscribers with various self-service channels, such as interactive voice response, or IVR, internet site, automatic and live chat and live sms chat, facebook chat and our mobile phone application which enables our customers to monitor data usage, obtain digital monthly invoices, includes self-service tutorials, online assistance with internet service problems and chat with a service representative. We invest efforts in directing our customers toward self-service channels.

Customer service for our OTT TV and internet infrastructure market services (including our independent deployment of fiber-optic infrastructure) are provided also through technicians providing services at the customers' homes.

We constantly invest time and efforts making our services compatible to persons with disabilities, including as required by law. We provide customers with disabilities convenient accessibility to our premises and adapted services, including free dispatch services, text to speech services as well as support services through chat. We also train our representatives to provide accessible service to all our customers.

Marketing

Our marketing strategy emphasizes our position as a communications group and cellular market leader, our value for money and our provision of a comprehensive solution for our customers' communication needs, by offering bundles of services. We believe the provision of bundles, including triple and quatro play packages of our services strengthen loyalty and increase customer satisfaction. We aim to provide our customers with a comprehensive quality experience through the various means of communications that they use, including their mobile handset, tablet, laptop and television.

From surveys that we conduct from time to time, we learn that subscribers base their choice of communications provider primarily on the following parameters: the services included in the bundle; perceived price of services and handsets; level of customer service; perceived quality of the network; general brand perception; with regards to the cellular provider - selection of handsets and their compatibility with their needs and with regards to the TV service provider – the quality and variety of content. Our marketing activities take into consideration these parameters and we invest efforts to preserve our subscriber base and attract new subscribers.

We leverage our extensive interactions with our customers to provide the requested services and also to cross- and up-sell cellular and fixed line products and services according to customer needs, usage trends and profitability, mostly by using advanced CRM system models, to increase customer satisfaction, loyalty and revenues.

We regularly advertise in all forms of media, specifically in digital media and television, using our familiar and loved advertising language which contributes to our brand's strength and popularity.

We believe that our strong brand recognition gives us the high level of market exposure required to help us achieve our business objectives.

Competition

Competition – General

The principal competitive factors in the telecommunications market include the services included in the bundle, perceived price, general brand perception and customer service.

In response to the enhanced competition in the Israeli telecommunications market, we have implemented various steps and strategies, including:

- identifying new opportunities to maximize our advantages as a communications group, such as our successfully launched OTT TV services, internet infrastructure services through the landline wholesale services and our investment in fiber-optic and IOT;
- focusing on the offering of bundles of services such as our successfully launched triple and quatro play offerings, as it strengthens customer retention and on enlarging customer purchases from us;
- entering network sharing and hosting agreements with Golan and Xfone, facilitating a more efficient cost structure in relation to our networks and operations thereof and investments therein;
- deploying fiber-optic infrastructure independently or advancing the investment in IBC , in relation thereof, in order to reduce our costs and dependency on Bezeq and Hot;

- investing in our network to ensure our ability to offer quality and advanced cellular and fixed line services, and providing our customers with advanced services; and

- taking aggressive efficiency measures through adjustments to our existing head count, reducing overhead expenses and improving work processes, in order to reduce costs and improve our agility.

Our ability to compete successfully will depend, in part, on our ability to anticipate and respond to trends and events affecting the industry, including the introduction of new services and technologies, changes in consumer preferences, demographic trends, economic conditions, pricing strategies of competitors and changes to the legal and regulatory environment.

Competition may intensify further as a result of the occurrence of any of the events described under “Item 3. Key Information – D. Risk Factors – Risks Related to our Business – We face intense competition in all aspects of our business.”

Communications groups and structural separation

The Israeli telecommunications market is currently dominated by four communications groups: Bezeq, Hot, Partner and Cellcom. Each of the Bezeq and Hot groups are subject to certain structural separation requirements in relation to sale of bundles of services by each of them and their respective subsidiaries, as a result of being the incumbent and monopoly in their respective core business – landline and multichannel television services. Those requirements include Bezeq's obligation to offer some of the services in its bundle separately under the same terms as in the bundle, and the requirement that Bezeq allow its competitors to participate in a similar bundle (if it includes internet connectivity, VOB or ILD services) under the same terms and equally markets such bundles as its own bundle (though the second requirement does not apply to the sale of the bundle by a subsidiary of Bezeq). The same requirements apply to Hot in the case of bundles that include internet connectivity services, with respect to the internet connectivity service component of the bundle.

Following a certain relaxation of the structural separation imposed on the Bezeq group, Bezeq is allowed to offer bundles of services with its subsidiaries under certain conditions, and in 2015 Bezeq merged with Yes (a company providing multichannel pay-TV) (detailed under "-Fixed line Segment – Television services" below). Bezeq's subsidiaries are allowed to sell and market each other's services, including through bundles of their services. Although the Hot group is also subject to structural separation limitations between its multi-channel television, connectivity, cellular and landline services, it was allowed to offer a bundle of landline telephony, multichannel television and internet infrastructure services and under certain conditions connectivity services as well, and Hot and Hot Mobile are also allowed to sell and market each other's services and exchange information. In January 2016 the Ministry of Communications announced its intention to annul Bezeq and Hot's structural separation as part of its plan to ensure massive investment in fiber optics infrastructure in Israel and in December 2016 the Ministry of Communication informed Bezeq that it intends to hold a public hearing regarding a possible annulment of the corporate separation and thereafter the structural separation in the Bezeq group and Bezeq has announced the commencement of a full merger process with Yes, including full integration of Yes into Bezeq. In 2018 Bezeq partially merged the operation of its subsidiaries – Pelephone, Yes and Bezeq International - thereby reinforcing their ability to compete with our triple offering, and withdrew its application for the MOC's approval of their re-organization, asking the MOC to accelerate its decision regarding the cancelation of the structural separation limitations on the Bezeq group. In February 2019, Bezeq filed a petition with the Supreme Court of Justice, against the MOC, requesting the immediate cancellation of the structural separation imposed on Bezeq.

In February 2019, the MOC published a hearing proposing further relaxation of Hot's structural separation regarding marketing for business customers.

The current regulation may change. See also "Item 3. Risk Factors - We face intense competition in all aspects of our business".

Cellular Segment

There is intense competition in all aspects of the cellular communications market in Israel, with a penetration rate (the ratio of cellular subscribers to the Israeli population) of approximately 120%, representing approximately 10.4 million cellular subscribers at December 31, 2018, and the average annual churn rate in Israel in 2018 is estimated to be 37%, higher than the churn rates in other developed economies. We expect this intensified competition to continue in the future. We currently compete for market and revenue share with nine other cellular communications operators: five MNOs (Partner, Pelephone, Hot Mobile, Golan and Xfone) and four MVNOs (Rami Levy Hashikma Communications Marketing Ltd., or Rami Levy, Azi Communications Ltd., or Azi, Free Telecom Ltd., or Free Telecom and Cellact Communications Ltd., or Cellact). The competition in the cellular market further increased after the entry of Xfone into the market in April 2018. Under the 4G tender terms, Xfone, Golan and Hot Mobile are eligible for up to a 50% discount on the license fees paid for the 4G frequencies, 10% for each 1% addition to their market share, obtained over a period of 5 years. For details of our network sharing and hosting agreements with Golan and Xfone, see "– Network and Infrastructure – Cellular Segment – Network sharing agreements" above.

Our estimated market share based on number of subscribers was approximately 27% as of December 31, 2018. The market shares at such time of Partner, Pelephone, Hot Mobile, Golan and Xfone were estimated to be approximately 25%, 21%, 15%, 8.6% and 1%, respectively, and the MVNOs' collective market share was estimated to be 2.2%. These estimates are based on the public reports of other operators and our estimate of the market share of the operators who do not publish reports.

Hot Mobile and Golan commenced their UMTS operations in 2012. Rami Levy, Azi, Free Telecom and Cellact, all MVNOs, commenced operations in 2011 - 2013. Xfone commenced its operations in 2018.

Partner started operations in 1998 and is controlled by S.B. Israel Telecom Ltd. (indirectly controlled by the media entrepreneur Haim Saban). In March 2011, Partner purchased the outstanding shares of 012 Smile Telecom Ltd., or Smile Telelcom, an ISP and ILD operator, now also serving as Partner's cellular low cost brand dealer, and in 2015, its network sharing agreement with Hot Mobile was approved and the two companies began joint operation through a joint subsidiary.

Pelephone is a wholly-owned subsidiary of Bezeq, and started operations in 1986. As of January 2015, its low cost brand services are sold by another subsidiary of Bezeq – Walla Communications Ltd., an internet portal. Bezeq is controlled by B Communications Ltd., or B Communications,. B Communications is an Israeli company traded on the NASDAQ and the TASE. Currently, B Communications' controlling shareholder is in the process of a debt restructuring in the Israeli court.

Hot Mobile operated in the cellular market as of 2001. In 2012 it began its UMTS operation. Hot Mobile is owned by Hot, which is owned by the French businessman Mr. Patrick Derhy. In 2015, its network sharing agreement with Partner was approved and the two companies began joint operation through a joint subsidiary.

Golan is owned by Electra, a public Israeli company that distributes and retails consumer products and is part of a large Israeli business group. Golan began to operate in 2012. For details of our network sharing and hosting agreements with Golan and Xfone, see "-Network and Infrastructure – Cellular Segment – Network sharing agreements" above.

Xfone is controlled by Xfone Communications Ltd., an Israeli ISP, which is owned by the Israeli businessman Hezi Bezalel.

Rami Levy is a subsidiary of a major Israeli discount supermarket chain. Azi is owned by Telzar, an ILD operator. Cellact is owned by Cellact Ltd., a content provider. Free Telecom is owned by an Israeli business man.

Israel is a small country (approximately 9 million residents) with 10 cellular operators and aggressive competition and regulation which led to some of the lowest cellular prices worldwide. Competition may remain in its current heightened condition or even increase and prices shall remain low, unless the market undergoes substantial changes.

Handsets

In the handsets market, we compete with numerous vendors, chain stores and importers' stores, and expect this trend to continue and include also global companies. Competition in this market has increased significantly in recent years and decreased sales for us. See "Item 3.Risk Factors - Our handsets revenues and profitability decreased further in 2018 and may continue to decrease" for additional details. Competition in this market may increase further.

Fixed-line Segment

The only groups having their own nation-wide landline infrastructure in Israel are Bezeq and Hot. We are dependent on Bezeq and Hot's broadband services for the supply of our internet services. The growing demand for data capacity increased our dependency on Bezeq's wholesale services. In 2014, a third competitor – IBC - commenced deployment of its infrastructure on the IEC's fiber optic infrastructure in selected areas, and in 2016 and 2017, respectively, Partner and we began extending our existing independent fiber optic infrastructures into residential areas. Should our investment in IBC and IBC becoming a widespread alternative to Bezeq be effected, this would improve our competitiveness in the fixed-line services market as this is likely to reduce our dependency on Bezeq and reduce our costs. For more details, see " – Networks and Infrastructure – Fixed-line Segment – Fixed-line Infrastructure " and thereunder "- Investment in IBC" above.

A landline wholesale market was formally launched in Israel in 2015 but to date, only internet infrastructure (BSA) and to some extent physical infrastructure services are provided on Bezeq's infrastructure and the wholesale market on Hot's infrastructure is in initial stages. See "-Government Regulations – Fixed-line Segment – Wholesale Landline Market" below.

An effective wholesale landline market, specifically one providing both telephony and infrastructure services, would enhance our ability to compete and extend our service offering. However, an annulment or substantial alleviation of corporate or structural separation and Bezeq's tariffs supervision, or further consolidation of Bezeq's subsidiaries, may have a material adverse effect on our competitive capabilities and results of operation, especially if effected before an effective wholesale market is in place. The consolidation of Bezeq's subsidiaries may have an adverse effect on our ability to grow in our triple and quatro offering. Further, the entry of new competitors to the fixed-line market, through the wholesale market, has increased competition in the fixed-line market and may trigger further escalation in the competition in other markets in which we operate.

Internet Infrastructure and Connectivity Business

The two main internet infrastructure providers for the private sector in Israel and offering internet infrastructure services to both ISPs and end-users are Bezeq and Hot. Bezeq, and as of 2018 Hot as well, are also providing internet infrastructure services to operators that do not own their own infrastructure under the landline wholesale market, who, in turn, provide this service to the end customer. IBC provides broadband services in selected areas through agreements entered into with some of the smaller ISPs. IBC's licenses allow the provision of broadband infrastructure services to other licenses holders as well as directly to large business customers. Bezeq, Hot, we and Partner provide transmission services to business customers over each operator's respective independent transmission network. Partner started offering internet infrastructure services over its independent fiber optic infrastructure to the private sector in 2017. In 2018, we started offering internet infrastructure services in residential areas in which we deployed our independent fiber optic infrastructure as a stand alone service or as part of our triple and quatro offerings.

As of September 30, 2018, internet infrastructure services were provided by Bezeq and Hot to approximately 1.05 million and 711,000 households in Israel, respectively, with an immaterial quantity by IBC. As of the first half of 2015, internet infrastructure services were provided by other operators, including us, through the landline wholesale market, using Bezeq's infrastructure and as of 2018 also using Hot's infrastructure. Based on Bezeq and Hot reports, at the end of September 2018, the internet infrastructure services household penetration rate was approximately 94%. We bundle this service with our internet connectivity service and also as part of our triple and quatro play offering. As of December 31, 2018, we had approximately 269,000 households subscribed to our end-to-end internet services. In 2018, Hot commenced providing wholesale landline services (maximum tariffs for Hot's wholesale internet infrastructure services are higher than those set for Bezeq's services). Effective inclusion of Hot's infrastructure in the wholesale market may increase the amount of potential subscribers to our triple and quatro play and bundle offerings.

Internet connectivity access is currently provided by three major ISPs: us, Bezeq International, Partner, and some other smaller players including Hotnet (a subsidiary of Hot) and Xfone Communications Ltd. (Xfone's controlling shareholder).

The Israeli internet connectivity market is highly competitive and saturated. As of the date of this report, there are a few dozen ISPs in Israel, though most of them do not hold significant market shares. Competition among the various players concentrates mainly on pricing.

The offering of bundles of services and the aggressive campaigns of both Bezeq and Hot offering substantially higher bandwidth for lower tariffs to end-users, resulted in a substantial decrease in internet connectivity service prices and led to increased demand for greater bandwidth, which required us to increase the capacity we purchase from Bezeq and Hot. Further, the offering of bundles of internet infrastructure and connectivity using the wholesale market increased the competition in this field, resulted in loss of some of our internet connectivity customers. Bezeq's breach of its obligation to market our connectivity services when proposing an internet infrastructure and connectivity bundle until April 2018 also resulted in a substantial loss of connectivity business. If competition remains at current levels and the regulatory environment remains unchanged, this trend is expected to continue to have a material adverse effect on our results of operations.

Global internet connectivity is provided by three underwater cables. The main provider, which also provides us with global internet connectivity, is TI Sparkle, and two additional underwater cables are owned by each of Tamares Telecom and the Bezeq group.

Television services

Multichannel pay-TV services are dominated by Hot (the incumbent TV provider and monopoly in this field) and YES (a subsidiary of Bezeq) with approximately 777,000 and 587,000 households, respectively, as of September 30, 2018. The multichannel pay-TV market is also highly penetrated. We successfully entered this market in December 2014, using an hybrid OTT-DTT television service and have approximately 219,000 households subscribed to our Cellcom tv services as of December 31, 2018. In June 2017 Partner launched its OTT TV solution and has approximately 106,000 households subscribers as of September 30, 2018. In August and October 2017, respectively, Hot and Yes each launched an OTT TV low cost brand solution – branded Hot Next and Sting, respectively (Hot's OTT TV solution is also marketed by Rami Levy). Partner's OTT TV solution includes Netflix's (internet based VOD content provider) application integration (and offering for a limited period). Hot's offer also includes Netflix's application integration. Also, Netflix and Amazon Prime, another internet based VOD content provider, provide their services to viewers in Israel, as complementary service to the existing competitors' content. We expect this trend to continue and include additional global players and also local participants.

Under the Israeli Antitrust Commissioner's 2014 instructions, aiming to facilitate the entry of new competitors to the TV market by reducing entry barriers, preconditions for the approval of any merger in the Bezeq group were published, including the requirements that Bezeq is to generally not bill ISPs for TV related internet infrastructure services and annul and not engage in any non-original production exclusivity arrangements.

ILD services

We are a major service provider in the Israeli ILD market. As of the date of this report, there are several ILD operators in the Israeli market. Our main competitors in this market are Bezeq (through its wholly-owned subsidiary Bezeq International) and Partner (through a wholly-owned subsidiary). Additional competitors include Xfone, Telzar International Communications Services Ltd., Rami Levy, Golan and Hot, through wholly-owned subsidiaries or affiliates. At the end of September 2018, our market share in the ILD market is estimated to be approximately 27%.

The Israeli ILD market is highly competitive, and the competition in the market is based mainly on the operator's ability to offer attractive pricing and to bundle this service with additional services such as cellular services.

In recent years the use of free of charge alternative technologies such as voice-over-IP has resulted in downsizing of the telephony market, especially the ILD services revenues. This trend is expected to continue in the future.

Landline telephony

The Israeli landline telephony market has been dominated for many years by Bezeq, the incumbent landline monopoly, which held as of December 31, 2017 (according to the Ministry of Communications report) approximately 2/3 of the landline telephony market (and an even larger revenues market share in the business landline telephony sector(. Hot, the incumbent TV monopoly, was the second entrant to this market. Other players include us, Partner's subsidiary and Bezeq International.

We offer landline telephony to selected business customers and landline telephony using VOB technology to private customers. We estimate that our current market share in the Israeli landline telephony market is not material. In case landline telephony is effectively included in the landline wholesale market, we may also offer landline home telephony services to private customers based on the wholesale market.

The landline wholesale market was to allow wholesale landline telephony service as of May 2015. In June 2017 the Ministry of Communications allowed Bezeq not to offer wholesale landline services until July 2018 and to provide a resale telephony service (at substantially higher tariffs) as a temporary substitute. In June 2018, the MOC resolved not to prolong Bezeq's temporary resale telephony as an alternative for its obligation to provide wholesale landline telephony services after the lapse of the temporary alternative period and to obligate Bezeq to provide wholesale landline telephony services as of August 1, 2018. Both Bezeq and Hot have expressed willingness to provide wholesale telephony services, but to date, no such service has been provided. For details, see "– Government Regulation – Fixed-line Segment – Wholesale landline market".

Other fixed-line services

Transmission and landline data services are provided by Bezeq, Hot, Partner and us. These services are provided to business customers and to telecommunications operators. During 2018 , the competition in these fields of operation intensified following HOT's and Partner's offerings, and the usage of bandwidth of transmission increased.

IOT services are provided by Bezeq, Pelephone and other software integration companies and additional participants are entering this field. We offer a wide range of advanced IOT services and solutions, through cooperation with leading IOT technology and services vendors. The IOT market is characterized by intense competition and includes the offerings of communications providers which offer both connectivity solutions and end-to-end solutions and large software integration companies.

Intellectual Property

We are a member of the GSM Association, together with other worldwide operators that use GSM technology. As a member of the association, we are entitled to use its intellectual property rights, including the GSM logo and trademark.

We are the proprietor of over 160 domain names and approximately 100 trademarks and trademarks applications, the most important of which are the star design, “Cellcom”, “Talkman”, “Cellcom Volume,” "Cellcom tv," "Netvision" and "013 Netvision". We are also the proprietor of a few registered patents.

Government Regulations

The following is a description of various regulatory matters that are material to our operations, including certain future legislative initiatives that are in the process of being enacted. There can be no certainty that the future legislation described here will be enacted or that it will not be subject to further change before its final enactment.

General

A significant part of our operations is regulated by the Israeli Communications Law, 1982, the regulations promulgated under the Communications Law and the provisions of our licenses, which were granted by the Ministry of Communications pursuant to the Communications Law. We are required by the Communications Law and the Wireless Telegraph Ordinance (New Version), 1972, to have a license in order to provide certain communications services in Israel and be allocated the spectrum to do so.

See also “Item 3. Key Information – D. Risk Factors – We operate in a heavily regulated industry, which can harm our results of operations. Regulation in Israel has materially adversely affected our results. ”

Cellular Segment

Our Cellular license

We provide our cellular services under a non-exclusive general license granted to us by the Ministry of Communications in June 1994, which requires us to provide cellular services in the State of Israel to anyone wishing to subscribe. The license expires on January 31, 2022, but may be extended by the Ministry of Communications for successive periods of six years, provided that we have complied with the license and applicable law, have continuously invested in the improvement of our service and network and have demonstrated the ability to continue to do so in the future. The main provisions of the license are as follows:

- the license may be modified, cancelled, conditioned or restricted by the Ministry of Communications in certain instances, including: if required to ensure the level of services we provide; if a breach of a material term of the license occurs; if any of our managers or directors is convicted of a crime of moral turpitude and continues to serve; or if we and our 10% or greater shareholders fail to maintain combined shareholders’ equity of at least $200 million; it is prohibited for any of our office holders or anyone holding more than 5% of our means of control, to hold, directly or indirectly, more than 5% of the means of control in Bezeq or another cellular operator in Israel, or to serve as an office holder of one of our competitors, subject to certain exceptions requiring the prior approval of the Ministry of Communications;

- the direct and indirect holdings of DIC and Koor (or a transferee or transferees approved by the Ministry of Communications), in the capacity as our founding shareholders, may not fall below 26% of our means of control (with "means of control" defined for these purposes as voting rights, the right to appoint a director or general manager, the right to participate in distributions, or the right to participate in distributions upon liquidation); the direct and indirect holdings of our founding shareholders who are Israeli citizens and residents may not fall below 5% of our means of control; at least 10% of our directors must be appointed by Israeli citizens and residents from among our founding shareholders and the majority of our directors must be Israeli citizens and residents;

- we or our office holders or a 5% or greater holder of any of our means of control may not commit an act or omission that adversely affects or limits competition in the cellular communications market;

- it is prohibited to acquire (alone or together with relatives or with other parties who collaborate on a regular basis) or transfer our shares, directly or indirectly (including by way of creating a pledge which if foreclosed, will result in the transfer of shares), in one transaction or a series of transactions, if such acquisition or transfer will result in a holding or transfer of 10% or more of any of our means of control, or the transfer of control over our company , without the prior approval of the Ministry of Communications. For the purpose of the license, "control" is defined as the direct or indirect ability to direct our operations whether this ability arises from our articles of association, from written or oral agreement or from holding any means of control or otherwise, other than from holding the position of director or officer;

- we are subject to the guidelines of Israel's General Security Services, which may include requirements that certain office holders and holders of certain other positions be Israeli citizens and residents with security clearance and the Minister of Communications is entitled under our license to appoint a state employee with security clearance to act as an observer in all meetings of our Board of Directors and its committees. If our service is to be determined by the Israeli Government to be an "essential service", the Prime Minister and the Ministry of Communications could impose additional limitations, including a heightened requirement of Israeli ownership of our ordinary shares;

- we are required to have agreements with a manufacturer of cellular network equipment for the duration of its intended operating period, which must include, among other things, a know-how agreement and an agreement guaranteeing the supply of spare parts for our network equipment for a period of at least seven years; we are required to interconnect our network to other public telecommunications networks in Israel, on equal terms and without discrimination and to provide national roaming services to Golan and Hot Mobile;

- we generally may not give preference in providing infrastructure services to a license holder that is an affiliated company over other license holders;
- there are certain general types of payments that we may collect from our subscribers, certain procedures and requirements for charging and collecting payments, general mechanisms for setting and raising tariffs, including the basic airtime charging units and prior notifications we must provide the MOC and our customers prior to increasing tariffs and the Ministry of Communications is authorized to intervene in setting tariffs in certain instances;
- we must maintain a minimum standard of customer service, including, among other things, operation of call centers, maintenance of a certain service level (both coverage and performance) of our network, protection of the privacy of subscribers; and certain limitations and requirements regarding the process and documentation of our marketing and sale interaction with our customers;
- we may not transfer, pledge or encumber the license or any assets used for implementing the license without the prior approval of the Ministry of Communications;
- we are required to obtain insurance coverage for our cellular activities. In addition, the license imposes statutory liability for any loss or damage caused to a third party as a result of establishing, sustaining, maintaining or operating our cellular network. We have further undertaken to indemnify the State of Israel for any monetary obligation imposed on the State of Israel in the event of such loss or damage. For the purpose of guaranteeing our obligations under the license, we have deposited a bank guarantee in the amount of NIS80 million with the Ministry of Communications, which may be forfeited in the event that we violate the terms of our license;
- we must maintain and follow additional requirements as to: business continuity plan and a disaster recovery plan and network sharing implementation, under which we may be accountable for violations attributed to the other sharing partners; and
- we are required to provide the Ministry of Communications information and reports upon its request, as well as detailed annual reports regarding various aspects of our operations.

In the event that we violate the terms of our license, we may be subject to substantial penalties, including monetary sanctions under the Communications Law, the sum of which shall be calculated as a percentage of our income and based on the gravity of the breach. The maximum amount per violation that may be imposed is approximately NIS 1.6 million plus 0.225% of our annual revenue for the preceding year, subject to criteria published by the Ministry of Communications. In recent years the MOC has substantially increased its supervision activities and imposed monetary sanctions, including on us (in immaterial amounts). Substantial sanctions will harm our results of operations. In the event that we materially violate the terms of our licenses, the Ministry of Communications has the authority to revoke them.

In May 2018 and again in March 2019, the MOC amended our licenses to regulate the manner of response of call centers, including measurable parameters for response times. The amendment shall come into force in July 2019. Also in July 2019, an amendment to the Israeli Consumer Protection Law regulating the manner of response of call centers will also come into effect. The amendment includes measurable parameters for response times, which are partly incompatible with the said amendment to our licenses. These amendments had and are expected to continue to have an adverse effect on our results of operations.

Services in Judea and Samaria

The Israeli Civil Administration in Judea and Samaria granted us a non-exclusive license for the provision of cellular services to the Israeli-populated areas in Judea and Samaria. This license is effective until 2022. The provisions of the cellular license described above, including as to its extension, generally apply to this license.

Tariff supervision

Interconnect tariffs among landline operators, international call operators and cellular operators are subject to regulation.

In case of a disagreement as to the terms of a hosting service (including the consideration), whether for national roaming of a new MNO (currently Golan, Hot Mobile and Xfone) or hosting of an MVNO, the regulators may intervene in the terms of the agreement, including by setting the price of the service. Unfavorable terms and consideration for the hosting service, may result in material adverse effect on our results of operations. For additional details, see "– Mobile Virtual Network Operators" below.

The Minister of Communications is authorized to give instructions and to set interconnect tariffs and usage of another operator's network rates and supervised services prices, based not only on cost plus reasonable profit, but also on the basis of comparison to other licensees, comparable services or such services or interconnect tariffs in other countries. In addition, the Minister of Communications was authorized to give instructions in relation to structural separation for the provision of different services, including between services provided to a licensee and services provided to a subscriber.

Mobile virtual network operators

A mobile virtual network operator, or MVNO, is a cellular operator that does not own its own spectrum and usually does not have its own radio network infrastructure. Instead, MVNOs have business arrangements with existing cellular operators to use their infrastructure and network for the MVNO's own customers. See also "– Tariff Supervision" above.

To date, the Ministry of Communications has granted approximately 20 MVNO or unified licenses (which also allow the provision of cellular services as MVNO). Four MVNOs are currently active.

Network Sharing

Network sharing is conditioned upon certain conditions, including: (i) other operators may be allowed to join on terms similar to the terms granted to the sharing operator with the smallest market share; (ii) each sharing operator may host a MVNO without the other sharing operators' consent; (iii) the shared radio network must be operated through a joint entity held equally by the sharing operators, which entity will be required to obtain a license from the MOC and will use the frequencies allocated to sharing operators; and (iv) the radio elements of the shared network will be held in equal parts by the sharing operators, and each of the sharing operators will have the right to use other sharing operators' passive infrastructure including following termination of the agreement.

For details regarding our network Sharing Agreements, see "– Network and Infrastructure – Cellular Segment – Network sharing agreements".

Permits for cell site construction

General

In order to provide and improve network coverage to our subscribers, we depend on cell sites located throughout Israel. The regulation of cell site construction and operation are primarily set forth in the Israeli National Zoning Plan 36 for Communications, or the Plan, and in the Communications Law.

The construction and operation of cell sites are subject to permits from various government entities and related bodies, including:

- building permits from the local planning and building committee or the local licensing authority (if no exemption is available);
- approvals for construction and operation from the Commissioner of Environmental Radiation of the Ministry of Environmental Protection;
- permits from the Civil Aviation Authority (in most cases);
- permits from the Israel Defense Forces (in certain cases); and
- other specific permits necessary where applicable, such as for cell sites on water towers or agricultural land.

National Zoning Plan 36

The Plan includes guidelines for constructing cell sites in order to provide cellular broadcasting and reception communications coverage throughout Israel, while preventing radiation hazards and minimizing damage to the environment and landscape and sets forth the considerations that the planning and building authorities should take into account when issuing building permits for cell sites. The Plan also determines instances in which the public must be informed of requests for building permits prior to their issuance, so that they may submit objections to the construction of a site. Following contradicting decisions by appeal and national zoning committees, in November 2018 the Supreme Court resolved that amelioration charges may be charged in relation to building permits issued in reliance on a national zoning plan . Such decision limits our ability to oppose the charges of amelioration charge in connection to our cell sites and may substantially increase the costs of constructing a site.

If the Plan is amended so as to include additional restrictions and requirements on the construction and operation of cell sites, this will harm our ability to construct new cell sites, make the process of obtaining building permits for the construction and operation of cell sites more cumbersome and costly, and could adversely affect our existing network and delay the future deployment of our network.

Site licensing

We have experienced difficulties in obtaining some of the permits and consents required for the construction of cell sites, especially from local planning and building authorities. The construction of a cell site without a building permit (or applicable exemption) constitutes a violation of the Planning and Building Law, which is criminal in nature. The Planning and Building Law contains enforcement provisions to ensure the removal of unlawful sites. As of December 31, 2018, we were subject to three criminal and administrative legal proceedings alleging that some of our cell sites were built and have been used without the relevant permits or not in accordance with the permits. As of the same date, a small portion of our cell sites operated without building permits or applicable exemptions. Although we are continually seeking to obtain building permits for these sites, we may not be able to obtain them and in several instances we may be required to relocate these sites to alternative locations or to demolish them without any suitable alternative. In addition, we may be operating a significant number of our cell sites, in a manner which is not fully compatible with the building permits issued for them, although they are covered by permits from the Ministry of Environmental Protection in respect of their radiation level. In some cases we will be required to relocate these cell sites to alternative locations, to reduce capacity coverage or to demolish them without any suitable alternative.

Based on advice received from our legal advisors and consistent with most court rulings on the matter and the Israeli Attorney General's opinion on the matter that the exemption from obtaining a building permit applies to cellular radio access devices, we have not requested building permits under the Planning and Building Law for rooftop radio access devices. In the course of petitions against the Attorney General's opinion and our and other operators' appeals against certain contrary decisions of the District Court against us and other operators, the Attorney General concluded that the application of the exemption does not balance properly the different interests involved and therefore cannot continue forward. At the Attorney General's request, the Israeli Supreme Court issued in 2010 an interim order which prevents cellular operators from constructing further radio access devices in cellular networks in reliance on the exemption until the enactment of regulations setting conditions for the application of such an exemption or other decision by the court, other than the replacement of existing radio access devices under certain conditions. In October 2018, regulations setting procedures for the construction, changes to and replacement of radio access devices exempt from building permits, or the 2018 Regulations, were enacted. Although these regulations reflect previous judicial limitations placed upon our ability to make changes and replace radio access devices in 2010, they also introduce a new licensing procedure that may further reduce our ability to construct new radio access devices based on such exemption. This may adversely affect our existing networks and our networks' build-out. In December 2018, following the enactment of the 2018 Regulations, petitions against the Attorney General's opinion were dismissed and our and other operators' appeals against certain contrary decisions of the District Court were accepted.

Other legal proceedings relating to the exemption, including as to its application to rooftops located at the same level as a place of residence or otherwise regularly frequented, were decided against our position, and others, including as to the requirement to obtain an extraordinary usage permit in certain circumstances, including as to the radio access devices' ancillary equipment, are still under consideration. While the Company is of the opinion that the exemption relates to such ancillary equipment and the 2018 Regulations supports its position, the Ministry of Justice expressed an opinion that such regulations and the exemption do not relate to the radio access devices' ancillary equipment. The Ministry of Justice is expected to publish further instructions in the matter. Other claims asserting that those cell sites and other facilities do not meet other legal requirements, continue.

Inability to rely on, or substantial limitation of, the exemption, the dismantling of radio access devices and cell sites due to reasons out of our control and the objection of some local planning and building authorities to grant due permits where required, or the exclusion of the ancillary equipment from the exemption, if adopted, could have a negative impact on our ability to obtain environmental permits for these sites, could negatively affect the extent, quality, capacity and coverage of our network (specifically in urban areas), and our ability to continue to market our products and services effectively and may have a material adverse effect on our results of operations and financial condition.

Radio access devices do receive the required permits from the Ministry of Environmental Protection. Several local planning and building authorities argue that Israeli cellular operators may not receive building permits in reliance on the current Plan, for cell sites operating in frequencies not specifically detailed in the frequencies charts attached to the Plan, although most of our and other operators' cell sites (including all 4G cell sites) operate in frequencies not specifically detailed in the Plan. In a number of cases, these authorities have refused to issue a building permit for such new cell sites, arguing that building permits for such cell sites should be sought through other processes (which are longer and cumbersome), such as an application for an extraordinary usage or under existing local specific zoning plans. Following conflicting district decisions regarding this claim, the matter is expected to be decided by the Supreme Court. Some of the frequencies to which we may be required to transfer (see " – Networks and Infrastructure – Cellular Segment – Spectrum Allocation") are not specifically detailed in the Plan. We believe that the Plan applies to all cell sites, whether or not they operate in specific frequencies.

If this approach escalates or should the Supreme Court rule against the Company, it would have a negative impact on our ability to deploy additional cell sites, which could negatively affect the extent, quality and capacity of our network coverage and our ability to continue to market our products and services effectively.

In addition to cell sites, we provide repeaters (also known as bi-directional amplifiers) and femto-cells to subscribers seeking a solution to weak signal reception within specific indoor locations. Based on advice received from our legal advisors, we have not requested building permits under the Planning and Building Law for outdoor rooftop repeaters, which are a small part of the repeaters that have been installed. It is unclear whether other types of repeaters and femto-cells require building permits. Some repeaters and femto-cells require specific permits and we receive such permits, and others require a general permit from the Ministry of Environmental Protection in respect of their radiation level, and we ensure that each repeater functions within the parameters of the applicable general permit. Should it be established that the installation of repeaters and femto-cells requires a building permit, we will perform cost-benefit analyses to determine whether to apply for permits for new and existing repeaters and femto-cells or to remove them.

In addition, we construct and operate microwave sites as part of our transmission network. The majority of microwave sites are exempted from receiving permits from the Ministry of Environmental Protection (due to their low output) or require a general permit in respect of their radiation level. Based on advice received from our legal advisors, we have not requested building permits for such microwave facilities on rooftops. If the courts determine that building permits are necessary for the installation of these sites, it could have a negative impact on our ability to obtain environmental permits for these sites and to deploy additional microwave sites and could hinder the extent, quality and capacity of our transmission network coverage and our ability to continue to market our landline services to our business customers (based on our own infrastructure) effectively.

Operating a cell site or a facility without the requisite permits or not in accordance with permits granted could subject us and our officers and directors to criminal, administrative and civil liability. Should any of our officers or directors be found guilty of an offence, although this has not occurred to date, they may face monetary penalties and a term of imprisonment. In addition, our sites or other facilities may be the subject of demolition orders and claims of breach of contract and we may be required to relocate cell sites to less favorable locations or stop operation of cell sites. This could negatively affect the extent, quality and capacity of our network coverage and adversely affect our results of operations.

Indemnification obligations

Under the Planning and Building Law, local building and planning committees require letters of indemnification from cellular operators indemnifying the committees for possible depreciation claims against the committees, as a condition for issuing a building permit for a cell site. The limitation period within which depreciation claims may be brought under the Planning and Building Law is the later of one year from receiving a building permit under the Plan and six months from the construction of a cell site. The Minister of Interior Affairs retains the general authority to extend such period further.

To date we have provided approximately 420 indemnification letters in order to receive building permits. Local planning and building committees have sought to join cellular operators, including us, as defendants in depreciation claims made against them even though indemnification letters were not provided. We were joined as defendants in a small number of cases. We expect that we will be required to continue to provide indemnification letters as the process of deploying our cell sites continues. As a result of the requirement to provide indemnification letters, we may decide to construct new cell sites in alternative, less suitable locations, to reduce capacity coverage or not to construct them at all, which could impair the quality of our service in the affected areas.

Environmental radiation issues

Under the Non-Ionizing Radiation Law, it is prohibited to construct and operate cell sites without construction and operating permits from the Ministry of Environmental Protection. Receiving a construction permit is a precondition to receiving a building permit from the planning and building committee and receiving a building permit or an exemption therefrom is a precondition for the receipt of an operating permit. For both permits, the applicant must present the means taken (including technological means) to limit exposure levels from each cell site or facility.

The validity of a construction permit is for a period not exceeding three months, unless otherwise extended by the Commissioner, and the validity of an operating permit is for a period of five years, subject to the submission of annual reports regarding radiation surveys of our cell sites and other facilities by third parties that were authorized to conduct such surveys by the Commissioner. These permits contain various conditions that regulate the construction and/or operating of cell sites, as the case may be. Our cell sites routinely receive both construction and operating permits from the Commissioner within the applicable time frames. In addition, Cellular operators are required to provide the Commissioner with online, ongoing data regarding the radiation level on each of their cell sites and other facilities. We provide the Commissioner with the requested data. See "– Site licensing" above for additional details in regards to obtaining a building permit or relying on an exemption.

The Non-Ionizing Radiation Law also regulates permitted exposure levels and provisions for supervision of cell site and other facility operation and grants the Commissioner authority to issue eviction orders if a cell site or other facility operates in conflict with its permit, and it imposes criminal sanctions on a company and its directors and officers for violations of the law. Failure to comply with the Non-Ionizing Radiation Law or the terms of a permit can lead to revocation or suspension of the permit, as well as to withholding the grant of permits to additional cell sites of that operator.

Positions of the Ministries of Communications, Health and Environmental Protection published in 2012 in relation to the various aspects of the provision of 4G services in Israel, include proposed limitations on usage and deployment in order to reduce exposure to non-ionizing radiation. Such limitations were not included in later documents issued by the MOC, allowing the provision of 4G services and awarding 4G frequencies to the cellular operators.

Any amendment to the Non-Ionizing Radiation Law and the Planning and Building Law that will prohibit or substantially limit the grant of permits under such laws, will, among other things, limit our ability to construct new sites (and if applied to existing cell sites, it will also limit our ability to renew operating permits for many of our existing sites), will adversely affect our existing networks and networks build out, specifically in urban areas, and could adversely affect our results of operations.

Handsets

The Israeli consumer protection regulations regulate the maximum permitted level of non-ionizing radiation from handsets, according to the European and the American standards. They also require cellular operators to attach an information leaflet to each handset package that includes explanations regarding non-ionizing radiation, the maximum permitted level of non-ionizing radiation and the level of radiation of that specific model of equipment. The Radiation Regulations further require that such information also be displayed at points-of-sale, service centers and on the Internet sites of cellular operators.

SAR levels are a measurement of non-ionizing radiation that is emitted by a hand-held cellular handset at its specific rate of absorption by living tissue. SAR tests are performed by the manufacturers on prototypes of each model of handset, not for each and every item. We include the information published by the manufacturer regarding SAR levels as we do not perform independent SAR tests for equipment and rely for this purpose on information provided by the manufacturers. As the manufacturers' approvals refer to a prototype handset, we have no information as to the actual SAR level of each specific item and throughout its lifecycle, including in the case of equipment repair. We inform our customers that there may be changes in the SAR levels in the event of equipment repair.

We obtain certain approvals from the Ministry of Communications and the Office of Standards in connection with the importation of handsets.

We are required to provide a warranty during the first year and maintain spare parts for certain end user equipment purchased from us, for certain malfunctions for certain periods. We are also required to annul equipment sales in certain circumstances, at the request of the customer.

Fixed-line Segment

Our Fixed-line Licenses

Our Unified license

The establishment and operation of fixed-line communications networks, and allocation of spectrum if relevant, requires a license.

We provide landline telephone, ILD, internet connectivity and infrastructure services as well as a "network end point" services, under a non-exclusive unified license granted to our wholly owned subsidiary - Cellcom Fixed Line Communications Limited Partnership - in 2015. The license expires in 2026 but may be extended by the MOC for successive periods of 10 years. The license requires a bank guarantee in the amount of NIS 5 million deposited with the Ministry of Communications. The provisions of our cellular license, including as to its extension, generally apply to the unified license, subject to certain modifications, including a 20% minimum Israeli holding requirement which can be waived by the Minister of Communications when the unified license operator is controlled by a general license holder (as was done in our case).

Services in Judea and Samaria

The Israeli Civil Administration in Judea and Samaria granted us a non-exclusive unified license for the provision of internet connectivity and infrastructure, ILD, landline and 'network end point' services to the Israeli-populated areas in Judea and Samaria. This license is effective until 2026. The provisions of the cellular license described above, including as to its extension, generally apply to this license, subject to certain modifications.

Data and transmission services

We hold a non-exclusive special license for the provision of local data communications services and high-speed transmission services only to Cellcom Fixed Line Communications Limited Partnership, effective until April 2021. Data and transmission services are being provided to our customers by Cellcom Fixed Line Communications Limited Partnership. The provisions of our cellular and unified licenses described above, including as to their extension, generally apply to this license, subject to certain modifications.

Fiber-optic network

The Communication Law provides operators certain privileges in the deployment of fiber-optic cables and exempts them (including auxiliary facilities) from the requirement to obtain building permits. The deployment in a public domain is subject to advanced notification to the occupier of the land and coordination with other infrastructure owners, and on private land, the consent of the owner of the land.

In addition, operators that do not own their own nation-wide landline infrastructure may use certain physical infrastructure of Bezeq and Hot, based on the wholesale landline market, and certain wholesale obligations are applied on all landline operators, including us. See "- Wholesale landline market" below.

See also "- Cellular Segment – Permits for cell site construction - Site Licensing" above for a discussion regarding microwave sites forming a part of our transmission network.

Wholesale landline market

A policy document regarding landline wholesale services published by the MOC in 2012 provided for the creation of an effective wholesale telecommunications access market in Israel and the gradual annulment of the structural separation in the Bezeq and Hot groups and its replacement with an accounting separation and change of the supervision on Bezeq retail tariffs to maximum tariffs rather than the current setting of fixed tariffs. The latter generally depends on the development of a wholesale market and the state of competition in the market, and with relation to television services, if there is a reasonable possibility of providing a basic package of OTT services providers without a national landline infrastructure.

In 2015, a wholesale landline market was formally launched in Israel in regards to internet infrastructure services and use of certain physical infrastructure by operators who do not own such infrastructure, following amendments to Bezeq's and Hot's licenses so as to include certain wholesale landline services, such as internet infrastructure services and wholesale landline telephony services and use of certain of their physical infrastructure by operators who do not own such infrastructure and promulgation of regulations setting the maximum tariffs of the wholesale landline services to be provided by Bezeq.

Although the wholesale market was formally applicable to Hot's infrastructure as well, Hot's infrastructure had been effectively excluded from the wholesale market, initially as the maximum tariffs for Hot's wholesale infrastructure service were not published by the MOC until June 2017 (and are higher than those set for Bezeq's service) and thereafter, due to disagreements with Hot as to the implementation of the service, which were resolved by the MOC. The Ministry of Communications resolved not to interfere with the tariffs Hot has set for its wholesale telephony service. Effective inclusion of Hot's infrastructure in the wholesale market may increase the potential subscribers to our triple play and bundle offerings.

In June 2017, the Ministry of Communications published regulations setting Bezeq's resale telephony service to be provided by Bezeq as of July 2017, as a temporary 14 month alternative for wholesale landline telephony service, and postponed Bezeq's obligation to offer wholesale telephony service until the lapse of said resale telephony service period. In June 2018, the MOC resolved not to prolong Bezeq's temporary alternative further and to obligate Bezeq to provide wholesale landline telephony services as of August 1, 2018. As of the date of this report, Bezeq does not provide the wholesale landline telephony services.

A hearing published by the MOC in 2014, which was further elaborated in 2017, proposing a method of inspecting whether Bezeq and Hot reduce their retail tariffs and thereby reduce the difference between the wholesale and retail tariffs ("margin squeeze") for certain landline services, aiming at reducing the profit of operators who do not own landline infrastructure and preventing their operation in the market, has not been concluded yet by the MOC.

An amendment to the Communications Law applies certain wholesale obligations on all landline operators, including us, and requiring all landline operators to grant all other landline operators access to their passive infrastructure (except IBC's passive infrastructure), the terms of which (with the exclusion of Bezeq and Hot, whose terms are set by the regulator) will be negotiated by the parties. For details of the Minister of Communications' authority to give instructions and set usage of another operator's network rates, see "–Government Regulation – Cellular Segment - Tariff supervision" above.

OTT TV

Television services over the Internet are currently not subject to specific regulation in Israel.

Pursuant to the 2016 recommendations of a committee for the regulation of broadcasting nominated by the Ministry of Communications, in July 2018, a new bill for the regulation of broadcasting was published and includes classification of audio visual providers into four categories and determination of the regulation applied to each category as follows: (i) a provider with annual revenues of up to NIS 350 million from subscription fees – no license is required and no specific regulation applied; (ii) license of a medium size operator - a provider with annual revenues over NIS 350 million from subscription fees, but under NIS 700 million, requires a license, which includes a gradual mandatory investment in original Israeli content in an amount of up to 8 percent of the provider's annual revenues from subscription fees, as well as regulation, inter alia, in regards to minor and minorities protection, forbidden broadcasts and cross ownership limitations and prohibition on the provision of advertisement; (iii) license of a large size operator - a provider with annual revenues over NIS 700 million from subscription fees, requires a license, which includes a mandatory investment in original Israeli content in an amount not less than 8% of its annual revenues from subscription fees, prohibition on the provision of advertisements as well as regulation, inter alia, in regards to minor and minorities protection, forbidden broadcasts, regulation relating to consumer protection, cross ownership limitations, limitation regarding owning and producing channels and providing basic channel package; and (iv) license of a significant operator - a provider that owns a managed network for the provision of contents will be bound, inter alia, in regards to broadcasting open channels and specific channels of audio–visual license holders. The bill includes limited regulation regarding sports broadcasting and is focused on audio-visual providers, where the content provided is mainly aimed at the audience in Israel and therefore is expected not to apply to foreign TV content providers operating in Israel, such as Netflix and Amazon prime video. The Company does not expect the bill, if enacted, to materially change the regulation that applies to the Company. The bill requires legislative proceedings in the Israeli parliament, which may include material changes to the bill. If the legislation adopted requires us to make additional investments or impose unfavorable regulation on our OTT TV service, or apply such regulation to us and not to other OTT TV providers, or usage of the DTT infrastructure, it may adversely affect our OTT TV business.

As of November 2017, the regulator allowed three TV commercial channels (two of which later merged into one channel) to broadcast their content in high definition over the internet and to Hot and Yes but not over the DTT broadcasting system. As a result, our TV customers and other DTT customers in Israel cannot obtain these three specific channels in HD (but rather in standard definition). We believe this decision is discriminatory and unreasonable and have filed a petition against this decision with Israel's High Court of Justice. See also "– Competition – Fixed-line Segment – Television services" above.

Securities administrative enforcement

Under the Israeli Securities Law, certain violations of certain securities and securities-related laws supervised by the Israeli Securities Authority, or ISA, may be enforced through administrative measures. The ISA may impose various civil enforcement measures, including financial sanctions, payment to the injured party, prohibition of the violator from serving as an officer or a director for a specified period of time, annulment or suspension of licenses, approvals and permits granted under such laws and agreed settlement mechanism as an alternative to a criminal or administrative proceeding. In case of a violation by a corporation, vicarious responsibility could be attributed to the chief executive officer in some cases, unless certain conditions have been met, including the adoption and implementation of procedures for the prevention of the violation. We adopted such procedures for the prevention of violations. In recent years, significant monetary sanctions, ranging up to several million NIS in individual cases, have been imposed by the Israeli Securities Law Administrative Enforcement Committee on several publicly traded companies and their affiliates for breach of the provisions of the Israeli Securities Law.

Contributing to the Community and Protecting the Environment

We and our employees have been contributing to the community since our inception. We consider contribution to the community in Israel an important component of our business vision and believe we have a responsibility toward the Israeli community, as we acknowledge that business leadership goes hand in hand with social leadership.

During 2018, 20% of our employees participated in volunteering activities in the community. Since 2016, we have partnered with an association supporting ALS patients and family members in various voluntary activities, including our employees' participation in a fundraising race for ALS patients and donation in said race, the donation of a service workshop to the ALS association social workers and employees regarding the importance of service and provision of excellent service and familiarizing ALS patients with mitigating advanced technologies.

We are aware of the importance of environmental protection. We seek to operate responsibly to continuously reduce negative impacts on the environment and the landscape, aiming at a better environmental performance than required by local law. We dedicate personnel, funds and technologies to reduce our ecological footprint , through activities such as efficient deployment of infrastructure subject to the applicable standards, recycling of electronic components and packages, reduction of paper usage by managed printing, reduction of pollutants' emissions and energy usage, collection of used batteries, provision of a monthly bill and other correspondence to our subscribers via e-mail or SMS, transfer to usage of environment friendly raw materials and separation between different types of waste in our repair services and purchasing of electricity produced by a private natural gas based power station.

C. ORGANIZATIONAL STRUCTURE

Our largest shareholder, Koor, is a wholly-owned subsidiary of DIC. DIC is a public Israeli company traded on the Tel-Aviv Stock Exchange, one of Israel's largest business groups. See footnote no. 1 to the table under “Item 7.A – Major Shareholders” for information on the holdings of DIC.

We and Cellcom Fixed Line Communications Limited Partnership (see "- Government Regulations - Fixed-line Segment - Our Fixed-line Licenses - Our Unified Licenses"), are incorporated in Israel. Cellcom Fixed Line Communications Limited Partnership and Dynamica Communications Chain Stores Ltd., our wholly owned dealer, are our significant subsidiaries.

D. PROPERTY, PLANT AND EQUIPMENT

Headquarters

In 2003, we entered into an agreement for the lease of our headquarters in Netanya, Israel. The leased property covers approximately 57,800 square meters, of which approximately 26,000 square meters consist of underground parking lots. The lease is in effect until December, 2022 and is renewable for two additional periods of five years each, upon our notice. As of 2015, we started subleasing part of the property, which currently amounts to a quarter of our headquarters to several sub-lessees for a period of up to five years, following the reduction in headcount in our headquarters. The sub-lessees have options to renew the lease for additional periods.

Netanya Property

In 2010, we entered into a lease agreement for our techno-logistic center, in Netanya, Israel. The leased property covers approximately 11,000 square meters. The lease is for a term of ten years from August 2011 and is renewable for an additional period of 5 years, at our option. In case we do not exercise the option we shall be required to pay approximately NIS 11 million. As of 2015, we started subleasing part of the property, which currently amounts to approximately 6,100 square meters of the leased property, for a period of five to six years. The sub-lessees have an option to renew the leases for an additional period subject to certain conditions.

Haifa and Rosh-Ha’ayin Properties

We lease a property in Haifa and a property in Rosh-Ha'ayin. We use these properties for offices, for call centers, for network servers and for equipment storage. The Haifa lease covers approximately 8,900 square meters, is in effect until December 2019, and is renewable for three additional periods of two years each, upon our notice. The Rosh-Ha'ayin lease covers approximately 3,300 square meters, is in effect until December 2019 and is renewable for four additional periods of two years each, upon our notice. We sublease part of the property in Rosh-Ha'ayin to our wholly-owned dealer and another subsidiary.

Electricity

In December 2010, we entered into an agreement with Ramat Negev Energy Ltd., which constructed a private power plant fueled by natural gas in Israel, and we commenced purchasing a portion of our electricity from it in 2014. Under the agreement, we committed to purchase electricity for the earlier of a period of 15 years from commencement of operations of the power plant or until January 2028, subject to our right to terminate the agreement after six years from the commencement of operations of the power plant under certain conditions.

Service Centers, Points of Sale and Cell Sites

As of December 31, 2018, we leased 74 service centers, points of sale and other facilities (including those operated by our wholly-owned dealer), which are used for sales and customer service. Such lease agreements are generally for periods of two to three years, with extension options that vary by location.

In addition, we lease from various parties, including the Israeli Land Authority, or ILA, municipalities and private entities sites for the establishment, maintenance and operation of cell sites for our cellular network. The duration of these lease agreements are generally for two to five years, with an option to extend the lease for successive similar periods and exit windows that enable us to terminate the agreement prior to its scheduled expiration. In some of the agreements, the lessor is entitled to terminate the agreement at any time without cause, subject to prior notice. Based on our past experience, we encounter difficulties in extending the term of approximately 5% of the lease agreements for cell sites, which at times results in our having to pay higher rent in order to remain in the same locations or to find alternative sites. This may aggravate given our network sharing agreements.

In addition, we lease a number of points of presence in Israel that are used for equipment and servers storage and other communications equipment for the provision of landline services, and storage space for our servers and equipment in London and Frankfurt.

Authorization Agreement with Land Regulatory Authorities

In June 2013, we renewed an authorization agreement with the ILA that authorizes us to use lands managed by the ILA for the establishment and operation of cell sites. The authorization agreement is effective until December 2019. The authorization agreement provides that subject to the receipt of approval from the ILA, we will be entitled to establish and operate cell sites on the lands leased to third parties throughout the agreement's term. We undertook to vacate at the end of the agreement's term all facilities installed in the authorized area unless the authorization period is extended. Under the authorization agreement, the ILA is entitled to revoke authorizations granted to us in certain circumstances.

ITEM 4A. UNRESOLVED STAFF COMMENTS

None.

ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following operating and financial review and prospects should be read in conjunction with “Item 3. Key Information – A. Selected Financial Data” and our consolidated financial statements and accompanying notes appearing elsewhere in this annual report. Our financial statements have been prepared in accordance with International Financial Reporting Standards, or IFRS, as issued by the IASB which differ in certain respects from U.S. Generally Accepted Accounting Principles, or U.S. GAAP.

This discussion contains forward-looking statements. We have based these forward-looking statements on our current expectations and projections about future events. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of many important factors, including those set forth under “Item 3. Key Information – D. Risk Factors” and elsewhere in this annual report.

A. OPERATING RESULTS

Overview

General

We are one of the four major communications groups in Israel and the largest provider of cellular communications services in Israel with approximately 2.851 million cellular subscribers as of December 31, 2018, with an estimated market share of 27%. In recent years we have increased our presence in the fixed line market, adding TV and internet infrastructure services (the latter through the landline wholesale market and, as of 2018, also over our independent fiber-optic infrastructure), to our veteran ISP and landline telephony (both inland and long distance).

We earn revenues and generate our primary sources of cash by offering a broad range of communications services, including cellular, Internet services (connectivity and infrastructure), TV services and fixed-line telephony services (inland and international), as well as by selling handsets and other end-user equipment.

As of 2016, as a result of business and regulatory changes, as well as the Group’s entry into new fields of operation in the fixed-line market, the Group’s management attention in general and its chief operating decision maker's attention in particular, have shifted to focus on two main fields of operations, “Cellular” and “Fixed-line.” Accordingly we adjusted our operating segments for reporting prior periods as of January 1, 2014, on a retroactive basis.

Our cellular segment’s services include basic cellular communications services and data transfer, download and upload, as well as text and multimedia messaging services and advanced cellular content services, which we provide through our 2G and 3G networks, covering substantially all of the populated territory of Israel, and our 4G network covering most of the population of Israel. We also provide international roaming services to our subscribers in 180 countries as of December 31, 2018 as well as to subscribers of foreign networks visiting Israel. We offer our subscribers a wide selection of handsets of various leading global manufacturers as well as extended warranty services on most handsets we offer. A significant portion of our revenues is derived from our network sharing agreement with Golan.

Our fixed-line segment’s services include landline telephony services, internet infrastructure (since May 2015, through the landline wholesale market and, as of 2018, also over our own fiber-optic infrastructure) , connectivity services (ISP), television services (since December 2014) (OTT TV), transmission services, international calling services (ILD) , end user fixed-line equipment and IOT services.

We sell our various services on a stand-alone basis or bundled with certain other services offered by us, including a triple play bundle of end-to-end internet service, landline telephony and TV services and a quatro bundle which includes the triple offering plus cellular services.

Our management evaluates our performance through focusing on our key performance indicators, which include among others: cellular subscribers and average revenue per user of cellular, or ARPU, internet and TV subscribers (households) – both stand alone and as a part of a bundle, adjusted EBITDA (as defined in "Results of Operations"), adjusted EBITDA as percentage of revenues, operating income, net income, cash flow from operating activities, Free Cash Flow*, , subscriber churn rate and handset sales and profitability. These key performance indicators are primarily affected by the competitive and regulatory landscape in which we operate and our ability to adapt to the challenges posed.

*Free cash flow is a non-IFRS measure and is defined as the net cash provided by operating activities (including the effect of exchange rate fluctuations on cash and cash equivalents) excluding a loan to Golan Telecom, minus the net cash used in investing activities excluding short-term investment in tradable debentures and deposits and proceeds from sales of such debentures (including interest received in relation to such debentures) and deposits.

Our operating results, profitability and cash flow have decreased significantly in the past several years, with a loss for 2018, mainly due to the intense competition resulting largely from regulatory developments intended to enhance competition in the Israeli telecommunications market, which caused significant price erosion in the prices charged for the provision of cellular services and a decrease from equipment sales. Our operating income in 2018 was NIS 74 million ($20 million), a decrease of 75.1% from NIS 297 million ($79 million) in 2017 and a decrease of 76.1% from NIS 310 million in 2016. We recorded a loss in 2018 of NIS 64 million ($ 17 million), compared to net income of NIS 113 million ($30 million) in 2017 and a net income of NIS 150 million ($40 million) in 2016. The Company's net cash from operating activities in 2018 amounted to NIS 770 million ($203 million), a decrease of 0.5% from NIS 774 million ($207 million) in 2017 and a decrease of 1.4% from NIS 781 million ($208 million) in 2016. As our business environment continues to be characterized by increased competition in the various markets in which we operate, these factors may continue to negatively impact our business, which may further adversely affect our results of operations and financial condition. More over, our financial condition may be more volatile than our competitors, due to our substantially larger amount of debt. Other impacts may include the need to reduce investments, in absolute terms and in comparison to our competitors, which may harm our competitive standing and potential future growth, adversely affect our ability to raise additional debt and refinance our existing debt or adversely affect the terms and price of such debt raising, which in turn may further adversely affect our financial condition and may require equity capital raising, if possible.

We intend to drive revenue primarily by: maximizing the benefits of our position as a leading Israeli telecommunications group; offering our customers full and comprehensive mobile and wireline solutions and bundles of services (including triple/quatro play) and enhancing our competitive capabilities; retaining our existing subscribers and attracting new subscribers; offering new services that are synergetic to our core businesses like IOT and growing wireline service revenues. Entering a new and penetrated market may require substantial investment and additional expenses. We intend to continue our efforts to optimize our costs by implementing further efficiency measures and reducing our expenses, including through the network sharing and hosting agreements we entered into with Golan and Xfone and by our agreements for investment in IBC, contemplated sale of our independent fiber-optic residential infrastructure to IBC and IRU in IBC's fiber-optic infrastructure, as they are expected to allow us to reduce our current landline wholesale payments to Bezeq, and adjust our operations to the changing market conditions. We cannot guarantee the success of these measures. For details of our Sharing Agreements, see "Item 4. Information on the Company –B. Business Overview – Network and Infrastructure – Cellular Segment – Network sharing agreements". For details of our fiber-optic activity see" Item 4. Information on the Company – B. Business Overview – Networks and Infrastructure – Fixed-line Segment – Fixed-line infrastructure" and "– Investment in IBC" thereunder.

In 2018, we entered into a collective employment agreement with the Company's employees' representatives and the Histadrut for a term of three years (2018-2020). In March 2019, the Histradrut announced a labor dispute at the Company. We are negotiating a new collective employment agreement with our employees' representatives and the Histadrut but cannot guarantee the outcome of such negotiations. See also "Item 3. Key Information – D. Risk Factors – Risks Related to our Business – The unionizing of our employees may impede necessary organizational and personnel changes, result in increased costs or disruption to our operation."

The Israeli telecommunications market is currently dominated by four communications groups: Bezeq, Hot, Partner and Cellcom, with the first two having a full landline infrastructure.

The communications market is primarily regulated by the Ministry of Communications. Regulatory changes have had material adverse effects on our results of operations in recent years, including by facilitating the entry of additional competitors into the cellular market which dramatically increased competition. Recent consumer related amendments to our licenses had a material adverse effect on our results of operations. Such and other future amendments, if implemented, may continue to materially adversely affect our results of operations, should we not succeed to mitigate such effects. See “Item 4. Information on the Company – B. Business Overview – Government Regulations".

Competition may increase further if: current trends continue, the landline wholesale market, launched in 2015, is ineffective; the structural separation imposed on the Bezeq and Hot groups or Bezeq's tariffs supervision is annulled or further relaxed or other unfavorable regulatory changes relating to the Bezeq and Hot groups are effected; new competitors enter the communications markets; we do not procure or deploy a widespread landline infrastructure or enter into cooperation to use such infrastructure with an operator which owns such infrastructure; or we do not purchase additional frequencies or purchase frequencies in an amount equal to our competitors or make the necessary investments in our networks or in our business in general. We have continually implemented aggressive efficiency measures in order to mitigate those adverse effects, which included voluntary retirement plans for employees. We intend to continue to implement changes in order to continue our efforts to mitigate the adverse effects of the increased competition in many areas in which we operate. We cannot guarantee the success of these measures. Moreover, unionization of our employees may impede the execution of such measures. See "Item 3. Key Information – D. Risk Factors – Risks Related to our Business - We face intense competition in all aspects of our business" and "-The unionizing of our employees may impede necessary organizational and personnel changes, result in increased costs or disruption to our operation", and "Item 4. Information on the Company - B. Business Overview – Competition" for additional details.

The construction and operation of our cell sites and other transmission facilities are highly regulated and require us to obtain various consents and permits. See “Item 4. Information on the Company – B. Business Overview - Government Regulations – Cellular segment – Permits for Cell Site Construction.” We have experienced difficulties in obtaining some of these consents and permits and our ability to rely on an exemption from obtaining a building permit was severely limited. Also, we may be operating a significant number of our cell sites in a manner not fully compatible with the building permits issued for them. Additional restrictions on the construction and operation of cell sites and other facilities have been enacted recently and may be enacted in the future or we may be required to demolish or relocate these cell sites and facilities, which may adversely affect our existing networks and networks build out, specifically in urban areas, may prevent us from meeting our license requirements and could adversely affect our results of operations.

Our profitability is also affected by other factors, including changes in our cost of revenues and selling, marketing, general and administrative expenses, including depreciation and financing expenses.

Our results are also impacted by currency fluctuations. While substantially all of our revenues are denominated in NIS, for 2018, approximately17 % of cash outflow was denominated in, or linked to, other currencies, mainly U.S. dollars. Changes to the Israeli CPI, may also impact our results as part of our debentures (Series F, H and J) and some of our expenses are linked to the Israeli CPI. Any devaluation of the NIS against the U.S. dollar or other foreign currencies will therefore increase the NIS cost of our expenses that are not denominated in NIS or are linked to those currencies and any increase in the Israeli CPI will increase the financial expenses associated with our debentures. We enter into derivative instruments to mitigate the effect of the various market risks associated with these expenses. See “Item 11 – Quantitative and Qualitative Disclosures About Market Risk.”

Further, we have incurred significant debt by issuing debentures and receiving loans, the aggregate outstanding principal amount of which as of December 31, 2018 was NIS 3,865 million. See “– Liquidity and Capital Resources– Debt Service” and "-Other Credit Facilities”.

Our dividend policy targets a distribution of at least 75% of our annual net income on a quarterly basis. In respect of 2016, 2017 and 2018, our board of directors chose not to declare dividends given the intensified competition and its adverse effect on our results of operations and in order to strengthen our balance sheet. We undertook limitations on our dividend distributions in connection to the issuance of our F through L debentures and other credit facilities. See “Item 8. Financial Information – A. Statements and Other Financial Information - Dividend Policy” and “- B. Liquidity and Capital Resources- Dividend payments” and "– Debt Service" and "– Other Credit Facilities".

As of January 1, 2017, we apply International Financial Reporting Standard (IFRS) 15 following early adoption thereof, and capitalize part of the salaries expenses and commissions related to customer acquisition costs. The application of this standard had a material positive effect on the Company's financial results for the years 2017 and 2018. The standard was applied using the cumulative effect approach as from the initial date of application.

As from January 1, 2018 we apply IFRS 9 regarding financial instruments, which replaced IAS 39. The standard was applied using the cumulative effect approach as from the initial date of application without amendment of the comparative data, other than with respect to certain hedging items, with an adjustment to the balance of retained earnings and other components of equity as of the initial date of application. For additional details see note 2-F to our financial statements.

Revenues

We derive our revenues in the cellular segment primarily from the sale of cellular network services (such as airtime and data surfing), including content and value added services, roaming services as well as revenues derived from network sharing and hosting services, handset sale and handset repair services. Roaming services include roaming charges that we bill to our subscribers for the use of the networks of our roaming partners outside Israel, to which we refer as outbound roaming, and charges that we bill to our roaming partners whose subscribers use our network, to which we refer as inbound roaming. Originating calls on our network and from interconnect revenues from other operators for calls terminating on our network.

Our revenues in the fixed-line segment are derived from the sale of fixed-line communications services which include: internet infrastructure (through the landline wholesale market, since February 2015 and, as of 2018, also based on our independent fiber-optic infrastructure) and connectivity services, OTT TV services (since December 2014), transmission services, provided to other operators and to Golan and Xfone according to our network sharing agreement, international calling services (ILD), landline telephony services, operator services and teleconferencing services and equipment sales that are related to this segment.

Our revenues from cellular services are usually affected by seasonality with the third quarter of the year characterized by higher roaming revenues due to increased incoming and outgoing tourism. Equipment sales of the fixed-line segment are usually higher in the fourth quarter.

Cost of revenues

The principal components of our cost of revenues are the purchase of equipment, interconnect fees, content cost, cell site leasing costs, salaries, transmission services cost, internet connectivity services cost, purchase of call minutes related mainly to international calling services, outbound roaming services fees and cost of Internet infrastructure. Our cost of revenues also includes depreciation of the cost of our network equipment, tv set-top boxes, amortization of our spectrum licenses and rights of use of communications lines. As of April 2017, our cost of revenues decreased as a result of our sharing partners', participation in operating costs according to the Network Sharing Agreements.

Selling and marketing expenses

Selling and marketing expenses consist primarily of sales force salaries and dealers' commissions, advertising, public relations and promotional expenses. We compensate our sales force through salaries and incentives. Since January 1, 2017 part of our customer acquisition costs (salaries and dealers commissions) are capitalized as a result of the early adoption of a new International Financial Reporting Standard (IFRS 15). Our selling and marketing expenses also include depreciation, mainly of leasehold improvements and equipment in our service centers and points of sales, and amortization of intangible assets related to the acquisition of subsidiaries.

General and administrative expenses

General and administrative expenses consist primarily of salaries and compensation, professional and consultancy fees, leases and maintenance of our offices, bad debt and doubtful accounts allowance, and other administrative expenses. Our general and administrative expenses also include depreciation and maintenance fees, mainly for our billing and information systems.

Other income and expenses

Other income and expenses consist primarily of expenses related to employee retirement plans in 2016 and 2018 and gain from the sale of a subsidiary in 2017.

Financing income and expenses

Financing income and expenses consist primarily of interest expense on long-term loans and interest on our debentures and other credit facilities, the interest income component of handset long-term installment sales, the effects of fluctuations in currency exchange rates, Israeli CPI adjustments related to the Israeli CPI-linked debentures, and income or losses relating to financial derivative instruments that do not qualify for hedge accounting according to IFRS. Financing income and expenses also include interest income on deposits, discount amortization associated with our debentures, and gains and losses from our current investment in tradable securities.

Income Tax

Generally, Israeli companies were subject to corporate tax on their taxable income at the rate of 25% for the 2016 tax year, 24% for the 2017 tax year and 23% for the 2018 tax year and onward.

Israeli companies are subject to capital gains tax at the corporate tax rate. A deferred tax asset or liability is created for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Results of Operations - Comparison of 2016, 2017 and 2018

The following table sets forth key performance indicators for the periods indicated:

	Year Ended December 31,			Change*	
	2016	2017	2018	2017 vs. 2016	2018 vs. 2017
Cellular subscribers at end of period(1) (in thousands)	2,801	2,817	2,851	0.6 %	1.2 %
Internet-customers (households) (end of period) (in thousands) (2)	156	222	269	42.3 %	21.2 %
TV - households (end of period) (in thousands) (2)	111	170	219	53.2 %	28.8 %
Churn rate of cellular subscribers(1)(3)	42 %	46 %	44 %	-	-
Average monthly revenue per cellular subscriber (ARPU) (1)(4) (in NIS)	63	57	51	(9.5)%	(10.5)%
Operating income (in NIS millions)	310	297	74	(4.2)%	(75)%
Net income(loss) (in NIS millions)	150	113	(64)	(24.7)%	na
Adjusted EBITDA(5) (in NIS millions)	858	853	660	(0.6)%	(22.6)%
Operating income margin(6)	7.7 %	7.6 %	2.0 %	(0.1PP)	(5.6PP)
Adjusted EBITDA margin(7)	21.3 %	22.0 %	17.9 %	0.7pp	(4.1pp)

* pp denotes percentage points and this measure of change is calculated by subtracting the 2016 measure from the 2017 measure and the 2018 measure from the 2017 measure, respectively.

(1) Cellular subscriber data refers to active subscribers. We use a six-month method of calculating our cellular subscriber base, which means that we add post-paid subscribers to our subscriber base upon their joining our services and prepaid subscribers upon charging a prepaid card and we deduct subscribers from our subscriber base after six months of no revenue generation and activity on our network and no data usage or less than NIS 1 of accumulated revenues from M2M (machine to machine) subscribers. The six-month method is, to the best of our knowledge, consistent with the methodology used by other cellular providers in Israel. The 2017 cellular subscriber base includes subscribers added as part of our purchase of the operations of an Israeli Mobile Virtual Network Operator, or MVNO, during the third quarter of 2017. As of the third quarter of 2018, we add M2M subscribers to the cellular subscriber base only upon first use instead of at the time of joining our service as was done until the change. This change did not have a material effect on M2M prior subscriber data.

(2) TV and Internet customers (households) refer to active subscribers. Internet households receive end-to-end internet service, including infrastructure (based on the wholesale landline market) and connectivity services.

(3) Churn rate is defined as the total number of voluntary and involuntary permanent deactivations of cellular subscribers in a given period expressed as a percentage of the number of cellular subscribers at the beginning of such period. Involuntary permanent deactivations relate to cellular subscribers who have failed to pay their arrears for the period of six consecutive months. Voluntary permanent deactivations relate to cellular subscribers who terminated their use of our services. Churn rate data is excluding the above mentioned removals of subscribers.

(4) Average monthly revenue per cellular subscriber (ARPU) is calculated by dividing revenues from cellular services for the period by the average number of cellular subscribers during the period and by dividing the result by the number of months in the period. Revenues from inbound roaming services and hosting and network sharing services are included even though the number of subscribers in the equation does not include the users of those roaming, hosting and network sharing services. Inbound roaming services, hosting and network sharing services are included because ARPU is meant to capture all service revenues generated by a cellular network. Revenues from sales of Subscription Repair Services are included because they represent recurring revenues generated by subscribers, but revenues from sales of handsets (which for purposes of this report may include other types of cellular end user equipment, such as tablets), Random Repair Services, and other services are not. We and industry analysts, treat ARPU as a key performance indicator of a cellular operator because it is the closest meaningful measure of the contribution to service revenues made by an average subscriber.

We have set out below the calculation of cellular ARPU for each of the periods presented:

	Year Ended December 31,		
	2016	2017	2018
	(In NIS millions, except number of subscribers and months)		
Revenues	4,027	3,871	3,688
less revenues from equipment sales	994	952	904
less other revenues not in ARPU*	881	949	1,061
Revenues used in ARPU calculation (in NIS millions)	2,152	1,971	1,723
Average number of subscribers	2,832,407	2,797,341	2,826,013
Months during period	12	12	12
ARPU (in NIS, per month)	63	57	51

* Other revenues include revenues from other communications services, mainly fixed-line revenues and repair services.

(5) Adjusted EBITDA is a non-IFRS measure and is defined as income before financing income (expenses), net; other income (expenses), net (excluding gain from the sale of a subsidiary and expense related to employee retirement plans); income tax; depreciation and amortization; and share based payments. We present adjusted EBITDA as a supplemental performance measure because we believe that it facilitates operating performance comparisons from period to period and company to company by backing out potential differences caused by variations in capital structure (most particularly affecting our interest expense given our significant debt), tax positions (such as the impact on periods or companies of changes in effective tax rates or net operating losses) and the age of, and depreciation expenses associated with fixed assets. Adjusted EBITDA should not be considered in isolation or as a substitute for operating income or other statement of operations or cash flow data prepared in accordance with IFRS as a measure of our profitability or liquidity. Adjusted EBITDA does not take into account our debt service requirements and other commitments, including capital expenditures, and, accordingly, is not necessarily indicative of amounts that may be available for discretionary uses. In addition, adjusted EBITDA, as presented in this annual report, may not be comparable to similarly titled measures reported by other companies due to differences in the way these measures are calculated.

The following is a reconciliation of adjusted EBITDA with net income and operating income:

	Year Ended December 31,		
	2016	2017	2018
	(In NIS millions)		
Net income(loss)	150	113	(64)
Financing expenses, net	150	144	144
Taxes on income (tax benefit)	10	40	(6)
Operating income	310	297	74
Other expenses (income), net (excluding gain from the sale of a subsidiary and expense related to employee retirement plans)	8	(1)	-
Depreciation and amortization	534	555	584
Share based payments	6	2	2
Adjusted EBITDA	858	853	660

(6) Operating income margin is defined as operating income as a percentage of total revenues for each of the applicable periods.

(7) Adjusted EBITDA margin is defined as adjusted EBITDA as a percentage of total revenues for each of the applicable periods.

The following table sets forth our consolidated statements of income as a percentage of total revenues from operations for the periods indicated:

	Year Ended December 31,		
	2016	2017	2018
Revenues	100.0%	100.0%	100.0%
Cost of revenues	67.1 %	69.2 %	72.2 %
Gross profit	32.9 %	30.8 %	27.8 %
Selling and marketing expenses	14.3 %	12.4 %	15.3 %
General and administrative expenses	10.4 %	11.0 %	9.8 %
Other (income) expenses, net	0.5 %	0.2 %	0.7 %
Operating income	7.7 %	7.6 %	2.0 %
Financing expenses, net	3.7 %	3.7 %	3.9 %
Income(loss) before income tax	4.0 %	3.9 %	1.9 %
Income tax	0.3 %	1.0 %	0.2 %
Net income(loss)	3.7 %	2.9 %	1.7 %

Revenues

	Year Ended December 31,			Change	
	2016	2017	2018	2017 vs. 2016	2018 vs. 2017
	(In NIS millions)				
Revenues	4,027	3,871	3,688	(3.9)%	(4.7)%

The decrease in revenues in 2018 compared with 2017 is attributable to a 10.3% decrease in service revenues in the cellular segment, and a 5% decrease in equipment revenues. The decrease in service revenues was partially offset by an increase in revenues from the fixed-line segment in the Internet and TV fields.

The decrease in revenues in 2017 compared with 2016 is attributable to a 3.8% decrease in service revenues, driven by a decrease in the cellular segment's service revenues and a 4.2% decrease in equipment revenues. The decrease in service revenues was partially offset by an increase in revenues from the fixed-line segment in the Internet and TV fields.

The following table sets forth the breakdown of our revenues for the periods indicated based on the various sources thereof:

	2016			2017			2018		
	Revenues (in NIS millions)	% of Total Revenues		Revenues (in NIS millions)	% of Total Revenues		Revenues (in NIS millions)	% of Total Revenues	
Service revenues:									
Cellular services	2,025	50.3	%	1,777	45.9	%	1,581	42.9	%
Land-line communications services*	871	21.6	%	1,004	25.9	%	1,068	29.0	%
Other services**	137	3.4	%	138	3.6	%	135	3.7	%
Total service revenues	3,033	75.3	%	2,919	75.4	%	2,784	75.5	%
Equipment revenues	994	24.7	%	952	24.6	%	904	24.5	%
Total revenues	4,027	100.0	%	3,871	100.0	%	3,688	100.0	%

* Consists of international calling services, landline telephony services, transmission services, hubbing services, internet services (ISP and internet infrastructure services) and TV services.

** Consists of repair services fees.

During 2018, service revenues (comprising 75.8% of total revenues) decreased 4.6%, compared with 2017. This decrease in service revenues resulted mainly from a 10.3% decrease in cellular service revenues resulting mainly from the ongoing erosion in the prices of these services. and from the difference between the national roaming services revenues and the revenues for rights of use in cellular networks according to the network sharing agreements as of the beginning of the second quarter of 2017 The decrease was partially offset by a 6.4% increase in the fixed-line service revenues resulting mainly from an increase in revenues from TV and internet services, as well as from fixed-line communications services provided according to the network sharing agreement with Golan which came into force as of the beginning of the second quarter of 2017.

During 2017, service revenues (comprising 75.4% of total revenues) decreased 3.8%, compared with 2016. This decrease in service revenues resulted mainly from a 12.2% decrease in cellular service revenues resulting mainly from the ongoing erosion in the prices of these services and from the difference between the national roaming services revenues and the revenues for rights of use in cellular networks according to the network sharing agreement with Golan. The decrease was partially offset by a 15.3% increase in the fixed-line service revenues resulting mainly from an increase in revenues from TV and internet services, as well as from fixed-line communications services provided according to the network sharing agreement with Golan which came into force as of the beginning of the second quarter of 2017.

Fixed-line service revenues totaled NIS 1,068 million in 2018 compared to NIS 1,004 million in 2017. This increase resulted mainly from an increase in revenues from TV and internet services, as well as of fixed-line communications services provided according to the network sharing agreement with Golan as of the beginning of the second quarter of 2017.

Fixed-line service revenues totaled NIS 1,004 million in 2017 compared to NIS 871 million in 2016. This increase resulted mainly from an increase in revenues from TV and internet services, as well as of fixed-line communications services provided according to the network sharing agreement with Golan, which was partially offset as a result of the deconsolidation of Internet Rimon Israel 2009 Ltd. (our indirect subsidiary), or Internet Rimon, following the sale of the Group's holdings in Internet Rimon in the second quarter of 2017.

During 2018, revenues from other services totaled NIS 135 million compared with a total of NIS 138 million in 2017.

During 2017, revenues from other services totaled NIS 138 million compared with a total of NIS 137 million in 2016.

During 2018, equipment revenues (comprising 24.5% of total revenues) decreased 5%, compared with 2017. This decrease resulted mainly from a decrease in the quantity of cellular segment end user equipment sold during 2018 as compared to 2017. This decrease was partially offset by an increase in end user equipment sales in the fixed-line segment.

During 2017, equipment revenues (comprising 24.6% of total revenues) decreased 4.2%, compared with 2016. This decrease resulted mainly from a decrease in the quantity of cellular segment end user equipment sold during 2017 as compared to 2016. This decrease was partially offset by an increase in end user equipment sales in the fixed-line segment.

The following table sets forth the breakdown of our revenues for the periods indicated based on the types of subscribers:

	2016			2017			2018		
	Revenues	% of Total Revenues		Revenues	% of Total Revenues		Revenues	% of Total Revenues	
	(in NIS millions)			(in NIS millions)				(in NIS millions)	
Individual	2,832	70.3	%	2,702	69.8	%	2,579	69.9	%
Business	971	24.1	%	992	25.6	%	946	25.6	%
Other*	224	5.6	%	177	4.6	%	163	4.5	%
Total	4,027	100.0	%	3,871	100.0	%	3,688	100.0	%

* Mainly consists of revenues from inbound roaming services, hosting services and network sharing services.

A breakdown of revenues according to types of subscribers (individual and business) during 2018 compared with 2017, shows a 4.6% decrease in revenues attributable to individual subscribers and a 4.6% decrease in revenues attributable to business subscribers. The decrease in the revenues attributable to individual subscribers resulted mainly from the ongoing erosion in the price of cellular services, resulting from the intensified competition in the cellular market. The decrease in revenues attributable to the business subscribers resulted mainly from the decrease in recurring revenue resulted mainly from the intensified competition in the cellular market.

A breakdown of revenues according to types of subscribers (individual and business) during 2017 compared with 2016, shows a 4.6% decrease in revenues attributable to individual subscribers and a 2.2% increase in revenues attributable to business subscribers. The decrease in the revenues attributable to individual subscribers resulted mainly from the ongoing erosion in the price of cellular services, resulting from the intensified competition in the cellular market. The increase in revenues attributable to the business subscribers resulted mainly from an increase in equipment revenues from that subscriber base.

The following table sets forth the breakdown of our revenues for the periods indicated based on the types of subscription plans:

	2016		2017		2018	
	Revenues (in NIS millions)	% of Total Revenues	Revenues (in NIS millions)	% of Total Revenues	Revenues (in NIS millions)	% of Total Revenues
Pre-paid	207	5.1 %	195	5.0 %	180	4.9 %
Post-paid	3,596	89.3 %	3,499	90.4 %	3,344	90.7 %
Other*	224	5.6 %	177	4.6 %	163	4.4 %
Total	4,027	100.0 %	3,871	100.0 %	3,688	100.0 %

* Mainly consists of revenues from inbound roaming services, hosting services and network sharing services.

A breakdown of revenues according to types of subscription plans (pre-paid and post-paid) during 2018 compared with 2017, shows a 4.4% decrease in revenues attributable to post-paid subscribers and a 7.7% decrease in revenues attributable to pre-paid subscribers. The decrease in revenues attributable to post-paid subscribers was primarily the result of the ongoing erosion in the price of cellular services, resulting from the intensified competition in the cellular market. The decrease in revenues attributable to pre-paid subscribers resulted mainly from increased churn of pre-paid cellular subscribers, as well as from the ongoing price erosion.

A breakdown of revenues according to types of subscription plans (pre-paid and post-paid) during 2017 compared with 2016, shows a 2.8% decrease in revenues attributable to post-paid subscribers and a 5.8% decrease in revenues attributable to pre-paid subscribers. The decrease in revenues attributable to post-paid subscribers was primarily the result of the ongoing erosion in the price of cellular services, resulting from the intensified competition in the cellular market. The decrease in revenues attributable to pre-paid subscribers resulted mainly from increased churn of pre-paid cellular subscribers, as well as from the ongoing price erosion.

Segment Revenues Discussion

We operate in two operating segments:

Cellular Segment – this segment includes the cellular communications services, cellular equipment and supplemental services.

Fixed-line Segment – this segment includes landline telephony services, internet infrastructure and connectivity services (ISP), television services, transmission services landline equipment and supplemental services.

These segments are managed separately for the purposes of allocating resources and assessing performance.

We started presenting our operations in these two segments as of January 1, 2016.

We measure revenues on an operating segment basis. The following is a discussion of our revenues for our two operating segments:

	Year Ended December 31,			Change	
				2017 vs.	2018 vs.
	2016	2017	2018	2016	2017
	(In NIS millions)				
Cellular service revenues	2,162	1,929	1,730	(10.8)%	(10.3)%
Cellular equipment revenues	836	770	655	(7.9)%	(14.9)%
Total cellular revenues	2,998	2,699	2,385	(10.0)%	(11.6)%
Fixed-line service revenues	1,071	1,166	1,215	8.9 %	4.2 %
Fixed-line equipment revenues	158	182	249	15.2 %	36.8 %
Total Fixed-line revenues	1,229	1,348	1,464	9.7 %	8.6 %
Consolidation adjustments	(200)	(176)	(161)	(12)%	(8.5)%
Consolidated revenues	4,027	3,871	3,688	(3.9)%	(4.7)%

Cellular Segment

Revenues from the cellular segment in 2018 totaled NIS 2,385 million (including inter-segment revenues), compared to NIS 2,699 million in 2017. The decrease was primarily due to a decline in service revenues of 10.3% resulting mainly from the ongoing erosion in the price of these services and from the difference between the national roaming services revenues until the end of the first quarter of 2017 and the revenues for rights of use in cellular networks according to the network sharing agreement with Golan which came into force as of the beginning of the second quarter of 2017 as well as a decrease in cellular equipment revenues of 14.9% compared to 2017.

Revenues from the cellular segment in 2017 totaled NIS 2,699 million (including inter-segment revenues), compared to NIS 2,998 million in 2016. The decrease was primarily due to a decline in service revenues of 10.8% resulting mainly from the ongoing erosion in the price of these services and from the difference between the national roaming services revenues in 2016 and the revenues for rights of use in cellular networks according to the network sharing agreement with Golan which came into force as of the beginning of the second quarter of 2017 and a decrease in cellular equipment revenues of 7.9% compared to 2016.

Fixed-line Segment

Revenues for the fixed-line segment (including inter-segment revenues) in 2018 totaled NIS 1,464 million, compared to NIS 1,348 million in 2017. This increase resulted mainly from an increase in revenues from TV and internet services, as well as of fixed-line communications services provided according to the network sharing agreement with Golan as of the beginning of the second quarter of 2017 and an increase in fixed-line equipment revenues.

Revenues for the fixed-line segment (including inter-segment revenues) in 2017 totaled NIS 1,348 million, compared to NIS 1,229 million in 2016. This increase resulted mainly from an increase in revenues from TV and internet services, as well as of fixed-line communications services provided according to the network sharing agreement with Golan.

Segment Adjusted EBITDA Discussion

We measure adjusted EBITDA on an operating segment basis. See note 6 to our financial statements included elsewhere in this report for details of this measure of segment profitability. We define segment adjusted EBITDA as income for a segment before financing income (expenses), net; other income (expenses), net (excluding gain from the sale of a subsidiary and expenses related to employee retirement plans); income tax; depreciation and amortization; and share based payments.

Cellular segment

In 2018, the cellular segment generated adjusted EBITDA of NIS 391 million compared to NIS 595 million in 2017, a 34.3% decrease. This decrease resulted mainly from the ongoing erosion in cellular service revenues.

In 2017, the cellular segment generated adjusted EBITDA of NIS 595 million compared to NIS 625 million in 2016, a 4.8% decrease. This decrease resulted mainly from the difference between national roaming services revenues in 2016 and the revenues for rights of use in cellular networks according to the network sharing agreement with Golan in 2017, and from the ongoing erosion in cellular service revenues. This decrease was partially offset by a decrease in selling and marketing expenses due to the capitalization of part of the customer acquisition costs as a result of the early adoption of a new International Financial Reporting Standard (IFRS15).

Fixed-line segment

In 2018, the fixed-line segment generated adjusted EBITDA of NIS 269 million compared to NIS 258 million in 2017, a 4% increase. The increase arose mainly as a result of an increase in revenues from internet and TV services as well as fixed-line communications services provided according to the network sharing agreement with Golan since the second quarter of 2017 .

In 2017, the fixed-line segment generated adjusted EBITDA of NIS 258 million compared to NIS 233 million in 2016, a 10.7% increase. The increase arose mainly as a result of an increase in revenues from fixed-line communications services provided according to the network sharing agreement with Golan and from a decrease in operating expenses. This increase was partially offset as a result of an erosion in the internet field profitability, as well as from the deconsolidation of Internet Rimon following its sale.

Cost of revenues and gross profit

	Year Ended December 31,			Change	
	2016	2017	2018	2017 vs. 2016	2018 vs. 2017
	(In NIS millions)				
Cost of service revenues	2,028	2,035	2,019	0.3 %	(0.8)%
Cost of equipment revenues	674	645	642	(4.3)%	(0.5)%
Total cost of revenues	2,702	2,680	2,661	(0.8)%	(0.7)%
Gross profit	1,325	1,191	1,027	(10.1)%	(13.8)%

The decrease in cost of service revenues in 2018 compared with 2017 resulted mainly from decrease in interconnect costs, depreciation and repair services This decrease was partially offset by an increase in costs of TV services content and in costs related to internet services in the fixed-line segment.

The decrease in cost of equipment revenues resulted mainly from a decrease in costs of end user equipment sold, primarily as a result of a decrease in the quantity of end user equipment sold in the cellular segment during 2018 as compared to 2017, which was partially offset by an increase in fixed-line equipment costs.

The increase in cost of service revenues in 2017 compared with 2016 resulted mainly from an increase in costs of TV services content and in costs related to internet services in the fixed-line segment. This increase was partially offset by a decrease in costs resulting from Golan's participation in operating costs according to the network sharing agreement with Golan.

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The decrease in cost of equipment revenues resulted mainly from a decrease in costs of end user equipment sold, primarily as a result of a decrease in the quantity of end user equipment sold in the cellular segment during 2017 as compared to 2016.

The decrease in gross profit in 2018 compared with 2017 resulted mainly from the ongoing erosion in the price of cellular services.

The decrease in gross profit in 2017 compared with 2016 resulted mainly from the ongoing erosion in the price of cellular services.

Selling and marketing expenses and general and administrative expenses

	Year Ended December 31,			Change	
	2016	2017	2018	2017 vs. 2016	2018 vs. 2017
	(In NIS millions)				
Selling and marketing expenses	574	479	567	(16.6)%	18.4 %
General and administrative expenses	420	426	360	1.4 %	(15.5)%
Total	994	905	927	(8.9)%	2.4 %

The increase in selling and marketing expenses in 2018 compared with 2017, is primarily the result of an increase in depreciation of acquisition costs that were capitalized as a result of the early adoption of a new International Financial Reporting Standard (IFRS 15) as of January 1, 2017.

The decrease in selling and marketing expenses in 2017 compared with 2016, is primarily the result of a decrease in salaries and commissions expenses due to the capitalization of part of the customer acquisition costs as a result of the early adoption of a new International Financial Reporting Standard (IFRS 15) as of January 1, 2017. The effect of the adoption of the standard on 2017 expenses was in a total amount of NIS 93 million ($27 million).

The decrease in general and administrative expenses in 2018 compared with 2017 resulted mainly from a decrease in salaries and related expenses as well as a decrease in doubtful debts..

The increase in general and administrative expenses in 2017 compared with 2016 resulted mainly from an increase in doubtful debts in 2017 compared to 2016.

Other income (expenses), net

	Year Ended December 31,		
	2016	2017	2018
	(In NIS millions)		
Other income (expenses), net	(21)	11	(26)

Other expenses in 2018 mainly includes expense of NIS 26 million following employee voluntary retirement plan executed in the second quarter of 2018. Other income in 2017 includes mainly a gain from the sale of a subsidiary (Internet Rimon) in the amount of approximately NIS 10 million.

Other income in 2017 mainly includes a gain from the sale of subsidiary Internet Rimon, in the amount of approximately NIS 10 million. Other expenses in 2016 primarily include an expense of NIS 13 million following an employee voluntary retirement plan executed in the second quarter of 2016.

Financing expenses, net

	Year Ended December 31,		
	2016	2017	2018
	(In NIS millions)		
Financing expenses	(196)	(196)	(190)
Financing income	46	52	46
Financing expenses, net	(150)	(144)	(144)

Financing expenses, net, for 2018 was similar to expenses, net, in 2017 and resulted mainly from losses in the Company's investment portfolio in 2018 due to capital market losses in the last quarter of 2018, which were offset by a decrease of the interest of debentures of the Company.

Financing expenses, net, for 2017 decreased 4.0% compared with 2016. The decrease resulted mainly from higher gains in the Company's investment portfolio in 2017 compared to 2016.

Income tax

	Year Ended December 31,			Change	
	2016	2017	2018	2017 vs. 2016	2018 vs. 2017
	(In NIS millions)				
Taxes on income(tax benefit)	10	40	(6)	400%	na

Taxes on income for 2018 totaled NIS 6 million as a result of the loss before taxes on income that the Company recorded in 2018, which was partially offset by tax expenses due to non-deductible expenses.

In January 2019, after the end of the reporting period, the Israeli Tax Authority issued a best judgment assessment for 2014 to the Company, generally due to timing differences. According to the assessment, if the Company's claims are rejected, the Company will be required to pay additional income tax in relation to the year 2014, in an amount of approximately NIS 56 million (including interest and Israeli CPI differences). The Company filed an objection to the tax assessment.

Taxes on income for 2017 increased 400% compared with 2016. This increase resulted mainly from the positive effects in 2016 of a tax assessment agreement for the years 2012-2013 and from recording income deferred tax in 2016 following a decrease in the corporate tax rate for the years 2017 and thereafter.

Net income (Loss)

	Year Ended December 31,			Change	
				2017 vs.	2018 vs.
	2016	2017	2018	2016	2017
	(In NIS millions)				
Net income (loss)	150	113	(64)	(24.6)%	na

The loss in 2018 totaled 64 million, primarily due to a decrease in operating profit mainly from the ongoing erosion in the price of cellular services.

The decrease in net income in 2017 compared with 2016, was primarily due to a decrease in operating profit mainly from the ongoing erosion in the price of cellular services and from a tax income in 2016, as a result of a tax assessment agreement for the years 2012-2013 and a decrease in corporate tax rate for the years 2017 and thereafter.

B. LIQUIDITY AND CAPITAL RESOURCES

General

Our liquidity requirements relate primarily to working capital requirements, debt service, capital expenditures for the expansion and enhancement of our networks, end user equipment and payment of dividends, to the extent declared. We fund these requirements through cash flows from operations, raising new debt and issuances of equity securities, including ordinary shares.

Since institutional investors were required to follow certain procedures and requirements pursuant to Israeli regulation before investing in non-governmental debentures, our series F and H through L indentures include certain limitations and covenants. For additional details see "– Debt Service" below. These limitations are generally also included in our other credit facilities (see "– Other Credit Facilities" below) and are expected to apply to any additional debt incurred by us. These procedures, limitations and covenants limit our freedom to conduct our business, may impose additional costs on us and may limit our ability to borrow additional debt from Israeli institutional investors as well as adversely affect the terms and price of such debt raising.

In May 2012 and June 2013, the rating of our debentures was downgraded. Though the rating of our debentures remained stable since then, any downgrade in our ratings may adversely affect the terms and price of our debt or additional debt raised, particularly through the issuance of debentures to institutional investors, which, given the limitation on the ability of Israeli banks to lend money to us pursuant to the "Guidelines for Sound Bank Administration" issued by the Israeli Supervisor of Banks (as for that purpose we are deemed to be included in the same group as DIC), may limit our ability to obtain additional financing to operate, develop and expand our business or to refinance existing debt. We believe that our sources of liquidity and capital resources, are adequate for our current requirements and business operations and should be adequate to satisfy our anticipated cash needs for working capital, capital expenditures, other current corporate needs and debt service for at least the next 12 months. Our future capital requirements will depend on many factors, including the level of revenues, the timing and extent of spending to support marketing and subscriber retention efforts, the expansion of sales and marketing activities and the timing of introductions of new products and enhancements of existing products, the level and timing of investing in our networks and services, including our OTT TV, internet infrastructure the investment in IBC and the purchase of additional frequencies and IOT services and any decision to reinstate dividends. Our Board of Directors would not expect to reinstate dividends unless it believes that our cash flow and available reserves will be sufficient to fund our needs, including our dividends. In February 2006, our Board of Directors adopted a policy to distribute each year at least 75% of our annual net income, on a quarterly basis, as dividends, subject to compliance with applicable law, our license and contractual obligations and so long as the distribution would not be detrimental to our cash needs or to any plans approved by our Board of Directors. We undertook limitations on dividend distributions in our indentures of series F and H through L debentures and in other credit facilities. See "Item 8. Financial Information – A. Consolidated Statements and Other Financial Information – Dividend Policy", "– Debt Service" and "–Other Credit Facilities" below. In respect of 2018, our Board of Directors chose not to declare dividends given the intensified competition and its adverse effect on our results of operations and in order to strengthen our balance sheet. It is possible that our Board of Directors' estimate of our cash needs will be incorrect, or that events could occur that could increase our cash needs beyond anticipated. If that occurs, we may not have sufficient cash to cover these needs as a result of various expenditures previously made by the Company, including prior investments and expenses and prior dividend payments, and we would need to identify additional sources of financing, which could include equity or debt financing. We may not be able to obtain such financing on acceptable terms or at all.

Dividend payments

In 2016, 2017 and 2018 our Board of Directors chose not to declare dividends given the intensified competition and its adverse effect on our results of operations and in order to strengthen our balance sheet.

Shelf Prospectus

In August 2017, we filed a shelf prospectus with the Israeli Securities Authority, or ISA, and the Tel Aviv Stock Exchange, or TASE. The shelf prospectus allows us, from time to time, until August 2019 (or if approved by the ISA, subject to certain conditions, until August 2020), to offer and sell various securities including debt and equity, in Israel, in one or more offerings, subject to filing a supplemental shelf offering report that describes the terms of the securities offered and the specific details of the offering and the prior approval of the TASE of the supplemental shelf offering report.

At this stage, no decision has been made as to the execution of any offering, nor as to its scope, terms and timing, if executed, and there is no certainty that such offering will be executed.

The shelf prospectus includes our undertaking to comply with certain reporting obligations under the Israeli Securities Law in the event of certain warning signs of financial stress.

Issuances of equity securities

In June 2018, the Company issued in an offering to the public in Israel only for a total net immediate consideration from the offering of approximately NIS 275 million:

- 12,121,200 ordinary shares of the Company (par value NIS 0.01 per share, or ordinary shares).
- 3,030,300 Series 1 Options. Each Series 1 Option entitled the holder thereof to purchase one ordinary share at an exercise price of NIS 19.50, until December 24, 2018. Series 1 Options were exercised for a total consideration of NIS 59 million.
- 3,030,300 Series 2 Options. Each Series 2 Option entitles the holder thereof to purchase one ordinary share at an exercise price of NIS 20, until June 24, 2019.

The offering was made in Israel only under the Company's Israeli 2017 shelf prospectus and the securities were registered for trading on the Tel Aviv Stock Exchange.

Debt service

Public debentures

Our Series F and G debentures were issued in March 2012 to the public in Israel under our 2011 shelf prospectus (as amended in March 2012) and were listed for trading on the Tel Aviv Stock Exchange. As of December 31, 2018, Series F debentures consisted of approximately NIS 429 million ($114 million) aggregate principal amount debentures (and in January 2019, we repaid a principal payment in the amount of approximately NIS 214 million ($57 million)) and Series G approximately NIS 86 million ($23 million) aggregate principal amount debentures (and in January 2019, we repaid Series G debentures in full).

The Series F principal is payable in four annual installments: one payment of 10% of the principal on January 5, 2017, and three equal annual installments of 30% of the principal, on January 5 of each of the years 2018 through 2020 (inclusive). The interest on Series F debentures is payable in semi-annual installments on January 5 and on July 5, of each calendar years commencing July 5, 2012 through January 5, 2020 (inclusive). Series F debentures bear an interest rate of 4.35% per annum, linked to the Israeli CPI for February 2012. In June 2013, following the ratings decrease discussed above, the annual interest rate for our Series F debentures was increased by 0.25% to 4.60%, beginning July 5, 2013.

The Series F debentures are unsecured and contain, in addition to standard terms and obligations, the following obligations:

- a negative pledge, subject to certain exceptions;
- a covenant not to distribute more than 95% of the profits available for distribution according to the Companies Law (“Profits”); provided that if our net leverage (defined as the ratio of net debt to EBITDA during a period of 12 consecutive months, excluding one-time events) exceeds 3.5:1, we will not distribute more than 85% of our Profits and if our net leverage exceeds 4.0:1, we will not distribute more than 70% of our Profits. For this purpose, net debt is defined as credit and loans from banks and others and debentures, net of cash and cash equivalents and current investments in tradable securities; and EBITDA is defined as profit before depreciation and amortization, other expenses or income, net, financing expenses or income, net and taxes on income;

- a limitation on our ability to voluntarily redeem the debentures prior to their stated maturity date to a minimum amount of NIS 100 million of each series of debentures and an undertaking to pay the holders of such debentures an additional annual interest of 1% in the event of such early redemption;

- a covenant to have the debentures rated by a rating agency (in as much as under our control);

- an obligation to pay additional interest of 0.25% for a two-notch downgrade in the debentures' rating and additional interest of 0.25% for each additional one-notch downgrade and up to a maximum addition of 1%, in comparison to the rating given to the debentures prior to their issuance;

- a covenant not to issue additional debentures of the relevant series if the additional issuance by itself, will cause a certain rating downgrade.

We also agreed to the addition of the certain events to the list of events of default of the Series F debentures, including:

- cross default, excluding following an immediate repayment initiated in relation to a liability of NIS 150 million or less;

- failure of our main business to be cellular communications or loss of our cellular license for a period of over 60 days;

- suspension of trading of the debentures on the TASE over a period of 45 days;

- failure to comply with the above covenant regarding limitations on dividend distributions;

- failure to have the debentures rated over a period of 60 days;

- a petition or court order to withhold all legal proceedings against us or petition for creditors arrangement filed;

- the sale of a major part of our assets or merger (with certain exclusions);

- failure to publish financial reports when due;

- a net leverage in excess of 5.0:1, or in excess of 4.5:1 during four consecutive quarters;

- failure to comply with our negative pledge covenant; and

- any other event causing or expected to cause a material adverse effect (which shall not include any event that shall or is likely to cause our net leverage to increase to a ratio of under 5.0:1) on our business and posing real threat of a substantial damage to the debenture holders’ rights.

Our Series H and I debentures were issued in July 2014 to the public in Israel under our 2014 shelf prospectus and were listed for trading on the Tel Aviv Stock Exchange. In February 2015, pursuant to an exchange offer under our 2014 shelf prospectus and in a private offering, we issued approximately NIS 844 million ($225 million) principal amount of Series H debentures and approximately NIS 335 million ($89 million) principal amount of series I debentures in exchange for approximately NIS 555 million ($148 million) principal amount of Series D debentures and approximately NIS 272 million ($73 million) principal amount of Series E debentures, respectively. Series D and Series E were fully repaid. In March 2016, we issued approximately NIS 246 million ($66 million) aggregate principal amount of additional Series I debentures to certain institutional investors in a private offering. As of December 31, 2018, our Series H and I debentures consisted of approximately NIS 836 million ($223 million) principal amount and NIS 724 million ($193 million) principal amount, respectively.

The Series H debentures principal is payable in seven annual installments: three equal annual installments of 12% of the principal on July 5 of the years 2018 through 2020 (inclusive), and four equal annual installments of 16% of the principal on July 5 of the years 2021 through 2024 (inclusive). The interest on the Series H debentures is payable in semi-annual installments on January 5 and on July 5, of each calendar year commencing on January 5, 2015 through July 5, 2024 (inclusive). The Series H debentures bear an interest rate of 1.98% per annum, linked to the Israeli Consumer Price Index for May 2014.

The Series I debentures principal is payable in eight annual installments: three equal annual installments of 10% of the principal on July 5 of the years 2018 through 2020 (inclusive), and five equal annual installments of 14% of the principal on July 5 of the years 2021 through 2025 (inclusive). The interest on the Series I debentures is payable in semi-annual installments on January 5 and on July 5 of each calendar year commencing on January 5, 2015 through July 5, 2025 (inclusive). The Series I debentures bear an interest rate of 4.14% per annum, without any linkage.

The Series H and I debentures are unsecured and contain, in addition to standard terms and obligations and the above undertakings in our Series F indenture which generally apply to our Series H and I debentures as well, the following obligations:

- in addition to being an event of default, meeting the financial covenants would be a condition for dividend distribution; and

- meeting the financial covenants would also be a condition for the issuance of additional debentures of each of the two new series.

The Series H and I Indenture contains substantially similar events of default to those included in the Series F Indenture, with the addition of certain events of default that do not appear in the Series F Indenture as well as certain modifications to the events of default that are included in the Series F Indenture, including:

- breach of the above limitation on dividend distributions;

- the minimum amount required for triggering a cross default shall not apply to a cross default triggered by another series of debentures;

- the existence of a real concern that we shall not meet our material undertakings towards the debenture holders;

- the inclusion in our financial statements during a period of two consecutive quarters of a note regarding the existence of significant doubt as to our ability to continue as a going concern; and

- breach of our undertakings regarding the issuance of additional debentures.

Our Series J and K debentures were issued in September 2016 to the public in Israel under our 2014 shelf prospectus and were listed for trading on the Tel Aviv Stock Exchange. In July 2018, we issued NIS 220 million ($59 million) principal amount of additional series K debentures in a private offering to certain Israeli institutional investors according to our June 2017 agreement with such investors. In December 2018, we issued approximately NIS 187 million ($50 million) principal amount of additional series K debentures to the public in Israel under our 2017 shelf prospectus. As of December 31, 2018, our Series J and K debentures consisted of approximately NIS 103 million ($27 million) principal amount and NIS 711 million ($190 million) principal amount, respectively.

The Series J debentures principal is payable in six installments, of which the first four installments of 15% of the principal each are payable on July 5 of the years 2021 through 2024, and the remaining two installments of 20% of the principal each are payable on July 5 of the years 2025 and 2026. The interest on the Series J debentures is payable on January 5 and on July 5 of each of the years 2017 through 2026. The Series J debentures bear interest at the rate of 2.45% per annum, linked to the Israeli Consumer Price Index for August 2016.

The Series K debentures principal is payable in six installments, of which the first four installments of 15% of the principal each are payable on July 5 of the years 2021 through 2024, and the remaining two installments of 20% of the principal each are payable on July 5 of the years 2025 and 2026. The interest on the Series K debentures is payable on January 5 and on July 5 of each of the years 2017 through 2026. The Series K debentures bear interest at the rate of 3.55% per annum, without linkage.

The Series J and Series K debentures are unsecured and contain standard terms and conditions in addition to certain additional undertakings by us generally similar to the terms of our Series H and Series I debentures.

Our Series L debentures were issued in January 2018 to the public in Israel under our 2017 shelf prospectus and were listed for trading on the Tel Aviv Stock Exchange. In December 2018, we issued approximately NIS 213 million ($57 million) principal amount of additional series L debentures to the public in Israel under our 2017 shelf prospectus. As of December 31, 2018, our Series L debentures consisted of approximately NIS 614 million ($164 million) principal amount.

The Series L debentures principal is payable in six installments, of which the first four installments of 15% of the principal are each payable on January 5 of the years 2023 through 2026, and the remaining two installments of 20% of the principal are each payable on January 5 of the years 2027 and 2028. The interest on the Series L debentures is payable on January 5 of each of the years 2019 through 2028. The Series L debentures bear interest at the rate of 2.5% per annum, without linkage.

The Series L debentures are unsecured and contain standard terms and conditions in addition to certain additional undertakings by us generally similar to the terms of our Series J and Series K debentures, with a change to the additional interest to be paid in case of a two-notch downgrade in the debentures' credit rating to 0.5% (with no change to the maximum additional interest).

As of December 31, 2018, we complied with the above covenants.

Other credit facilities

In May 2015, we entered into a loan agreement with two Israeli financial institutions, or Lenders, according to which the Lenders have agreed, subject to certain customary conditions, to provide us two deferred loans for the total principal amount of NIS 400 million ($115 million), without any linkage, as follows:

- A principal amount of NIS 200 million ($53 million) was provided to us in June 2016, and bears an annual fixed interest of 4.6%. The loan's principal amount is payable in four equal annual payments on June 30 of each of the years 2018 through 2021 (inclusive). The interest will be paid in ten semi-annual installments on June 30 and December 31, of each calendar year commencing December 31, 2016 through and including June 30, 2021. As of December 31, 2018, the outstanding principal amount under this loan is NIS 150 million ($40 million).

- A principal amount of NIS 200 million ($53 million) was provided to us in June 2017, and bears an annual fixed interest of 5.1%. The loan's principal amount is payable in four equal annual payments on June 30 of each of the years 2019 through 2022 (inclusive). The interest will be paid in ten semi-annual installments on June 30 and December 31, of each calendar year commencing December 31, 2017 through and including June 30, 2022.

Under the agreement, the interest rate may be subject to certain adjustments. We may cancel or prepay one or both loans, subject to a certain cancelation fee or prepayment fee, as applicable. The agreement includes standard terms and obligations and also generally includes the negative pledge, limitations on distributions, events of default and financial covenants applicable to our series F, H and I debentures.

In August 2015, we entered into a loan agreement with an Israeli bank, or Lender, according to which the Lender has agreed, subject to certain customary conditions, to provide us a deferred loan in a principal amount of NIS 140 million ($37 million), without any linkage, which was provided to us in December 2016, and bears an annual fixed interest of 4.9%. The loan's principal amount is payable in five equal annual payments on June 30 of each of the years 2018 through 2022 (inclusive), and the interest will be payable in 11 semi-annual installments on June 30 and December 30 of each calendar year commencing June 30,2017 through and including June 30, 2022. As of December 31, 2018, the outstanding principal amount under this loan is NIS 112 million ($30 million).

Under the Agreement, the interest rate may be subject to certain adjustments. We may prepay the loan, subject to a prepayment fee. The agreement also includes certain events which if not approved by the Lender allow the Lender to notify us of an acceleration of the repayment of the loan.

The agreement includes standard terms and obligations and also generally includes the negative pledge, limitations on distributions, financial covenants and event of defaults applicable to our series F, H and I debentures, with certain modifications, including foreclosure, materialization of a pledge, execution actions, receivership and (subject to certain exclusions) sale of assets in a specified certain lower amount, a failure to operate in a field which is material to our operations, and mergers and changes of formation (with more limited exclusions) will trigger an event of default. In case we provide stricter financial covenants to another financial institution or debenture holder, those will apply to this agreement as well.

In June 2017, we entered into an additional loan agreement with the Lender according to which the Lender has agreed, subject to certain customary conditions, to provide us a deferred loan in a principal amount of NIS 150 million ($40 million), unlinked, in March 2019, which will bear an annual fixed interest of 4%. The loan's principal amount will be payable in four equal annual payments on March 31 of each of the years 2021 through and including 2024 and the interest will be payable in ten semi-annual installments on March 31 and September 30 of each calendar year, commencing September 30,2019 through and including March 31, 2024. Until the provision of the loan, we are required to pay the Lender a commitment fee. The agreement includes similar terms and obligations to those included in our August 2015 loan agreement and applies the right to demand immediate repayment of either or both loans due to certain events of default under either agreement.

As of December 31, 2018, we complied with the above covenants.

In the ordinary course of business, from time to time, we and our subsidiaries, enter into framework agreements with banks for various banking services, such as credit lines and hedging transactions. In 2015, we entered into an extended payment terms agreement with a bank in relation to a certain supplier, which includes terms similar to our loan agreements and we allow such arrangements requested by our suppliers from time to time.

Capital expenditure

Our accrual capital expenditure in 2016, 2017 and 2018 amounted to NIS 382 million, NIS 550 million and NIS 647 million, respectively. Accrual capital expenditure is defined as investment in fixed assets and intangible assets, such as investments in our communications networks, fiber-optic infrastructure, information systems, software and TV set-top boxes and as from 2017, capitalization of part of the customer acquisition costs as a result of the early adoption of a new International Financial Reporting Standard (IFRS15).

Cash flows from operating activities

Cash flows from operating activities totaled NIS 770 million in 2018, a decrease from NIS 774 million in 2017. The decrease in cash flow is primarily attributed to a decrease in proceeds from customers due to the decrease in service revenues.

Cash flows from operating activities totaled NIS 774 million in 2017, a decrease from NIS 781 million in 2016. The decrease in cash flow is primarily attributed to a decrease in proceeds from customers due to the decrease in service revenues.

Cash flows from investing activities

The net cash flows from operating activities is the main capital resource for our investment activities. In 2016, 2017 and 2018, our net cash used in investing activities amounted to NIS 364 million, NIS 644 million and NIS 631 million, respectively. The payments were used primarily for the improvement and expansion of our networks, fiber-optic infrastructure and information systems. The decrease in 2018 compared with 2017 resulted mainly from a decrease in our current investments in debt securities and shares. The increase in 2017 compared with 2016 resulted mainly from higher cash capital expenditures in fixed assets and intangible assets and others in 2017 mainly due to the capitalization of part of the customer acquisition costs as a result of the early adoption of a new International Financial Reporting Standard (IFRS15) as compared to 2016 and of our current investments in tradable debentures.

Cash flows from financing activities

In 2018, net cash received in financing activities amounted to NIS 537 million compared to NIS 843 million used in 2017. The net cash we received is primarily attributable to issuances of debentures and equity offering in 2018.

In 2017, net cash used in financing activities amounted to NIS 843 million compared to NIS 62 million received in 2016. The net cash we used is primarily attributable to payments of principal and interest for our debentures.

Working capital

Our working capital as of December 31, 2018 was NIS 1269 million, compared with NIS 692 million as of December 31, 2017. The decrease in working capital was primarily due to an increase in cash and cash equivalents as a result of issuances of debentures and equity offering in 2018.

Our working capital as of December 31, 2017 was NIS 692 million, compared with NIS 1,074 million as of December 31, 2016. The decrease in working capital was primarily due to a decrease in cash and cash equivalents.

Trade receivables

Trade receivables consist of outstanding amounts due from customers, mainly for cellular, internet infrastructure and connectivity and landline telephony services and handsets and accessories, net of the allowance for doubtful accounts. Most of our handset sales are made on an installment basis (generally, 36 monthly payments). Installments due in the twelve months following the balance sheet date are included in current trade receivables; the remaining installments are included in long-term receivables. As of December 31, 2018, net current trade receivables amounted to NIS 1,152 million compared with NIS 1,280 million as at December 31, 2017 and NIS 1,325 million as at December 31, 2016. Net long-term trade receivables as of December 31, 2018 amounted to NIS 370 million compared with NIS 412 million as at December 31, 2017 and NIS 461 million as at December 31, 2016. The decrease in trade receivables (current and long-term) in 2018 compared with 2017 was mainly due to a decrease in service and equipment revenues. The decrease in trade receivables (current and long-term) in 2017 compared with 2016 was mainly due to a decrease in service and equipment revenues. . The current maturity of long-term receivables as of December 31, 2018 was NIS 466 million, compared with NIS 523 million as of December 31, 2017 and NIS 566 million as of December 31, 2016.

C. RESEARCH AND DEVELOPMENT, PATENTS AND LICENSES, ETC.

Not applicable.

D. TREND INFORMATION

Trend information is included throughout the other sections of this Item 5.

E. OFF-BALANCE SHEET ARRANGEMENTS

There are no off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources, except future commitments and agreements that are detailed in this report.

F. TABULAR DISCLOSURE OF CONTRACTUAL OBLIGATIONS

Set forth below is a description of our contractual cash obligations, in millions of NIS, as of December 31, 2018.

	Total	2019	2020-2021	2021-2022	2023 and Beyond
Long-term debt obligations (including interest)(1)	4,512	757	1,248	1,068	1,433
Operating lease obligations	741	283	316	119	23
Purchase obligations	452	275	138	39	-
Total	5,705	1,315	1,702	1,226	1,462

(1) Interest does not include any increase in interest that would be required based on increases in the Israeli CPI.

Application of Critical Accounting Policies and Use of Estimates

The preparation of our financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the amounts reflected in the consolidated financial statements and accompanying notes, and related disclosure of contingent assets and liabilities. We base our estimates upon past experience, where applicable, various factors, external sources and on other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions, and could have a material impact on our reported results.

In many cases, the accounting treatment of a particular transaction, event or activity is specifically dictated by accounting principles and does not require management’s judgment in its application, while in other cases, management’s judgment is required in the selection of the most appropriate alternative among the available accounting principles, that allow different accounting treatment for similar transactions.

We believe that the accounting policies discussed below are critical to our financial results and to the understanding of our past and future performance, as these policies relate to the more significant areas involving management’s estimates and assumptions. We consider an accounting estimate to be critical if: (1) it requires us to make assumptions because information was not available at the time or it included matters that were highly uncertain at the time we were making our estimate and (2) changes in the estimate or different estimates that we could have selected may have had a material impact on our financial condition or results of operations.

Long-lived assets – depreciation

Nature of critical estimate items

The communications industry is capital intensive. The depreciation of operating assets constitutes a significant operating cost for us. We have substantial investments in tangible long-lived assets, primarily our communications networks.

Assumptions / approach used

We depreciate our property, plant and equipment using the straight-line method. Separate individual significant components are depreciated over their individual estimated useful lives. We periodically review changes in our technology and industry conditions to determine adjustments to estimated remaining useful lives and depreciation rates.

Effect if different assumptions used

Changes in technology or changes in our intended use of these assets can cause the estimated period of use or the value of these assets to change. Actual economic lives may differ from estimated useful lives. Periodic reviews could result in a change in our assets' depreciable lives, and therefore, in our depreciation expense in future periods.

Impairment of long-lived assets

Nature of critical estimate items

Finite-lived long-lived assets

At each reporting date, we review finite-lived long-lived assets, principally consisting of property, plant and equipment, spectrum licenses and intangible assets for impairment based on the requirements of International Accounting Standard No. 36, whenever events or changes in circumstances indicate that their carrying values may not be recoverable through the present value of anticipated cash flows from the continued use of the asset, including those expected at the time of its future retirement and disposal. Where it is not possible to estimate the recoverable amount of an individual asset, we group together all of the assets that cannot be tested individually into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit"), and estimate the recoverable amount of the cash-generating unit to which the asset belongs. The recoverable amount is the higher of value in use and fair value less cost to sell. Value in use is determined by discounting the expected future cash flows, we expect to derive from the asset, using a pre-tax discount rate. An impairment loss is recognized if the carrying amount of an asset or cash-generating unit exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss.

Indefinite-lived intangible assets

Once a year and for the same date, or more frequently if there are indications of impairment, we estimate the recoverable amount of each cash-generating unit that contains goodwill. Cash-generating units to which goodwill has been allocated are aggregated so that the level at which impairment testing is performed reflects the lowest level at which goodwill is monitored for internal reporting purposes. We monitor goodwill at operating segments level. As regards cash-generating units that include goodwill, an impairment loss is recognized when the carrying amount of the cash-generating unit, after adjustment for goodwill, exceeds its recoverable amount.

Assumptions / approach used

In analyzing finite-lived long-lived assets and Indefinite-lived intangible assets for potential impairment, significant assumptions that are used in determining the discounted cash flows of the asset group include:

- cash flows attributed to the asset group;
- future cash flows for the asset group, including estimates of residual values, which incorporate our views of growth rates for the related business and anticipated future economic conditions; and
- period of time over which the assets will be held and used.
- Key assumptions used in the calculation of recoverable amounts are discount rate and terminal value growth rate.

Effect if different assumptions used

The use of different estimates and assumptions within our discounted cash flow models (e.g., terminal value growth rates, pre-tax discount rate, future economic conditions, estimates of residual values) could result in discounted cash flows that are lower than the current carrying value of an asset group, thereby requiring the need to reduce the carrying value to the discounted cash flow amount.

The use of different discount rates when determining the fair value of the asset group could result in different fair values, and impact any related impairment charges.

Change in estimates in finite-lived long-lived assets

- During the year ended December 31, 2017 management has updated estimates as follows: Towards the end of the Company's 2G and 3G frequencies (the "Frequencies") original amortization period, the Company's annual depreciation committee examined the estimated useful life of the Frequencies. Based on Company's estimate, the Company will continue to use the Frequencies at least for the next 10 years.

The estimated useful life of the Frequencies was determined in the past according to the period of the Company's cellular license (until 2022).

According to applicable law, the Company's cellular license may be extended for additional 6-year periods, subject to the requirements set in the license. The Company estimates that based on its experience and acquaintance with the communications market in Israel, if current conditions continue, there is high probability that the license will be extended for an additional term of 6 years.

In light of the aforesaid, the estimated useful life of the Frequencies has been re-evaluated for the first time, for an additional period of ten years, starting from the beginning of the second quarter of 2017 and ending in 2028 (instead of 18-20 years ending in 2022, as originally estimated).

Accounts receivable - bad debt and allowance for doubtful accounts

Nature of critical estimate items

We maintain an allowance for doubtful accounts to reflect estimated losses resulting from impairment of accounts receivables.

Assumptions / approach used

We regularly evaluate the adequacy of our allowance for doubtful accounts by taking into account variables such as past experience, age of the receivable balance and current economic conditions of the party owing the receivable balance. If the financial conditions of certain customers were to deteriorate, resulting in impairment in their ability to make payments, additional allowance for doubtful accounts may be required.

Effect if different assumptions used

We believe that our allowance for doubtful accounts is adequate to cover estimated losses in customer accounts receivable balances under current conditions. However, changes to the allowance for doubtful accounts may be necessary in the event that the financial condition of our customers improves or deteriorates.

Change in estimates

As from January 1, 2018 the Group applies IFRS 9, Financial Instruments The standard includes a new ‘expected credit loss’ model, which following its application, the amount of the provision for impairment of all the financial assets decreased by an amount of NIS 12 million as at January 1, 2018.

Provisions for contingent liabilities

Provisions in general are highly judgmental, especially in cases of legal disputes. We assess the probability of an adverse event as a result of a past event and if the probability is evaluated to be more likely than not and the amount of the obligation can be estimated reliably, we fully provide for the total amount of the estimated contingent liability. We continually evaluate our pending provisions to determine if additional accruals are required. It is often difficult to accurately estimate the ultimate outcome of a contingent liability. Different variables can affect the timing and amount we provide for certain contingent liabilities. Our provisions are therefore subject to estimates made by us having taken into consideration the opinion of our legal counsel, which are subject to changes as the status of legal and commercial disputes changes over time. Adverse revision in our estimates of the potential liability could materially impact our financial condition, results of operations or liquidity.

Uncertain tax positions

When assessing amounts of current and deferred taxes, we take into consideration the effect of the uncertainty that our tax positions will be accepted and the effect of incurring any additional tax and interest expenses. We are of the opinion that the cumulative tax liability is fair for all the years in respect of which final tax assessments have not yet been received, based on an analysis of a number of matters including interpretations of tax laws and our past experience. This assessment is based on estimates and assumptions that may also include assessments and exercising judgment regarding future events. It is possible that new information will become known in future periods that will require us to change our estimate regarding the tax liability that was recognized, and any such changes will be expensed immediately in that period.

Recognition of deferred tax asset in respect of tax losses

The Company assesses the probability that in the future there will be taxable profits against which carried forward losses can be utilized and accordingly the Company recognizes (or not recognizes) a deferred tax asset in respect of losses carried forward. In the absence of certainty for the existence of taxable income, deferred taxes are not recognized as an asset. The possible effects of this estimate is the recognition of additional income tax expenses.

New Accounting Standards Not Yet Adopted

For details regarding new accounting standards not yet adopted see note 3-R to our financial statements included elsewhere in this report.

ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

A. DIRECTORS AND SENIOR MANAGEMENT

The following table sets forth information regarding our directors, executive officers and other key employees as of December 31, 2018:

Name	Age	Position
Ami Erel (2), (3), (4)	72	Chairman of the Board
Mauricio Wior (2)	62	Vice Chairman of the Board
Shlomo Waxe (1), (2), (4)	73	Independent Director
Sholem Lapidot*	39	Director
Ephraim Kunda (1), (2), (4), (5)	66	Independent Director
Joseph Barnea (1), (2), (3), (4), (5)	83	Independent / External Director
Ronit Baytel (1), (2), (5)	51	Independent / External Director
Nir Sztern	48	President and Chief Executive Officer
Shlomi Fruhling	46	Chief Financial Officer
Yoni Sabag	46	Vice President of Marketing
Ron Shvili	51	Chief Technology Officer
Nadav Amsalem	45	Vice President of Business Customers
Sharon Amit	52	Vice President of Human Resources
Amos Maor	55	Vice President of Sales and Service
Liat Menahemi Stadler	52	Vice President of Legal Affairs and Corporate Secretary
Teimuraz Romashvili	40	Vice President of Pre Paid Activity
Yaniv Gruenwald**	44	Vice President of Television and Content
Ronnen Shles	51	Controller

(1) Member of our Audit Committee.
(2) Member of our Analysis Committee.
(3) Member of our Option Committee.
(4) Member of our Security Committee.
(5) Member of our compensation Committee.
* Since March 2018
**In March 2019, Mr. Yaniv Gruenwald resigned from office and will leave his position within the next few months.
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Ami Erel has served as Chairman of our Board of Directors since 2005. From 2014 to 2017 Mr. Erel provided consulting services to Discount Investment Corporation Ltd. (where he served as President and Chief Executive Officer from 2001 to 2013). Until 2011, Mr. Erel served a period as Chief Executive Officer and a period as Chairman of the board of directors. From 1997 to 1999, he served as President and Chief Executive Officer of Bezeq. From 2011 to 2016, Mr. Erel also served as Deputy Chairman of the Board of Directors of ADAMA Agricultural Solutions Ltd. (where he served from 2006 as a director and later as Chairman of the Board of Directors). Mr. Erel also serves as a director of Elron Electronic Industries Ltd. (where he served from 1999 to 2001 as President and until January 2007 as Chairman of the Board of Directors), Knafaim Holdings Ltd. and Dan hotels Ltd. Mr. Erel served as the chairman of the executive committee of the Manufacturers Association of Israel from 2005 to 2009 and from 2009 to 2011 he served as the chairman of the Israel Export & International Cooperation Institute. Mr. Erel holds a B.Sc. in electrical engineering from the Technion, Israel Institute of Technology.

Mauricio Wior has served as our Vice Chairman of our Board of Directors since January 2017. In January 2018, 2.5% of our outstanding share capital held by Koor was transferred (through a lending transaction) to a company controlled by Mr. Wior, following which Mr. Wior is considered joint controlling shareholder with Koor. Mr. Wior has served as Deputy Chairman of the Board of Directors of Shufersal Ltd. and of Israir Aviation and Tourism Ltd. since 2016, a member of the board of directors of IRSA Inversiones y Representaciones Sociedad Anónima, DIC's controlling shareholder, since 2006, a member of the board of directors of Banco Hipotecario in Argentina, a substitute director in DIC, the Company's indirect controlling shareholder, since 2014 and a member of the board of directors of additional private companies in Argentina. From 1990 to 2005, Mr. Wior served as the Chairman and CEO of cellular operators in Argentina, Uruguay, Chile, Ecuador, Peru and Venezuela, and as a senior executive of BellSouth Telecommunications, LLC. Mr. Wior holds a B.A in finance and accounting and an M.B.A. in Business Management, both from Tel Aviv University.

Sholem Lapidot has served as a member of our Board of Directors since March 2018. Mr. Lapidot serves as CEO of DIC, our indirect controlling shareholder, and of IDB. He also serves as a member of the board of directors of IDB, DIC and Shufersal Ltd., chairman of the board of directors of Modi'in - Energy Management (1992) Ltd., substitute director at Elron Electronic Industries Ltd., committee member at the IDB Fund and a member of the board of directors of additional private companies owned by DIC and IDB. Mr. Lapidot served as a member of the board of directors of ADAMA Agricultural Solutions Ltd. from 2015 to 2016, from 2009 to 2013 he served as the CEO and member of the board of directors of CLADD S.A. and from 2008 to 2012 as a member of the board of directors of Australtex S.A. Mr. Lapidot has studied Rabbinical Studies.

Shlomo Waxe has served as a member of our Board of Directors since 2006. Mr. Waxe has served as Director General of the Israel Association of Electronics and Software Industries from 2006 to 2016. Until 2016 he served as a member of the board of the Israeli Standards Institute. From 2002 to 2005, he worked in the field of communications management and consultancy. From 1999 to 2001, he served as Chief Executive Officer of Zeevi Communications Ltd. From 1997 to 1999, he served as a consultant to cellular communications projects in Sao Paulo, Brazil and in Northeast Brazil. From 1993 to 1997, he served as the Director General of Israel’s Ministry of Communications. From 1990 to 1993, he served as commanding officer of the signal, electronics and computer corps of the Israel Defense Forces and he is a retired brigadier general. Mr. Waxe also serves as a member of the boards of directors of C. Mer Industries Ltd. and until 2009, served as a board member of Shrem, Fudim – Technologies Ltd. and until May 2012, served as a board member of Tambour Ltd. Mr. Waxe holds a B.A. in political science from the University of Haifa.

Ephraim Kunda has served as a member of our Board of Directors since 2010. Mr. Kunda is an Israeli businessman and is the owner and managing director of a private consulting company that provides economic consultancy and business mediation services. From 2007 to 2010, Mr. Kunda has served as the Chairman of the board of directors and since 2010 as a member of the board of directors of Ravad Ltd., a public real estate investment company. From 2003 to 2007, Mr. Kunda served as an external director of Property and Building Corporation Ltd., a public real estate company controlled by DIC. Mr. Kunda holds a B.A. in Economics from Tel Aviv University.

Joseph Barnea has served as a member of our Board of Directors since 2007. Mr. Barnea is a retired businessman. From 2012 to 2015, Mr. Barnea served as an external director of Imagesat International Ltd. He served as the Chief Executive Officer of Oxygen & Argon Works Ltd. from 1987 to 2005 and continued to serve as a member of its management until 2006. From 1985 to 1987, he served as the Chief Executive Officer of Telkoor Ltd. From 1980 to 1985, he served as a Vice President of Elscint Medical Imaging Ltd. Mr. Barnea is a member of the executive committee of the Israeli Industrialists Association