

Tescom Software Systems Testing Ltd. (“Tescom” or “the Company”)

Interim Results for the Six Months Ended 30 June 2006

Tescom Software Systems Testing Ltd. (Symbol: TSCM), the international quality assurance and software testing service provider, announces its interim results for the six months ended 30 June 2006.

Highlights

- Revenues increased by 14.2% to \$26.8m, versus \$23.4m in H105
- Gross margins were 32.1%, compared to 37.7% in H105
- Profit before tax was \$1.1m, versus loss of \$0.1m in H105 (profit of \$1.1m, net of one-off items in 2005)
- Diluted earnings per share were \$0.05, versus loss of \$0.04 in H105
- New contract wins in the UK, France and Israel, with continued emphasis on long-term fixed-price projects
- Continued progress on landmark transaction as main contractor with the Ministry of Finance in France
- Strengthening of senior sales, delivery and marketing management in the UK, US and Israel

Ofer Albeck, CEO of Tescom, said: “Tescom’s H106 results reflect a significant increase in revenues over H105, particularly in the UK and in France. We look forward to a continuing positive trend in our top line throughout 2006, as we see the benefit of the reorganization and strengthening of our senior sales and management team. The market in Israel remains extremely competitive, which has had a negative effect on our gross margins and profitability. In addition, the loss of a major customer in Australia has also affected profitability.

Despite this, Tescom has won a number of major new contracts, including long-term fixed contracts in the public sector, from which we expect to benefit during the remainder of 2006.

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Chief Executive's Review

We are pleased to report that Tescom's H106 revenues increased by 14.2% from H105, to \$26.8m. Revenues increased in the UK, Continental Europe, Israel and in the Asia-Pacific region, mainly as a result of new large contracts in each of these locations, as well as a continued emphasis on improved management of existing accounts. Tescom's strategy is to continue focusing its efforts on large projects with fixed-price contracts, mainly in Europe and the US. During the period, the Company recorded significant progress on its three-year contract with the French Ministry of Finance, and the Company hopes to leverage its experience in this area in order to position itself to benefit from other public sector projects throughout Europe.

We are particularly pleased to report significant revenue increases in Europe. France nearly doubled its revenues in the first half of 2006 in comparison to 2005. In the UK, revenues have increased by over 17%, and Tescom has been successful at gaining new contracts in both the private and public sector. This has included working for the UK government departments that perform testing on projects being carried out by large systems integrators. In early 2006, BSkyB made Tescom their principal supplier for testing across the UK, and Vodafone announced its continuing relationship with Tescom, including the successful project regarding their "push e-mail" service.

Tescom continues to make progress in the US, despite a change in local management during the second quarter of 2006, and has won several long-term contracts in the state and local government sector. Revenues in the US remained relatively stable in the first half of 2006.

In the Asia-Pacific region, Tescom Singapore won a new contract with the Land Transport Authority of Singapore and Tescom Australia signed a new contract with the Victorian State Government. Revenues for the first half of 2006 reflected strong growth, mainly from a substantial increase in Singapore revenues, which was partially offset by a decline in Australian revenues due to a completion of a large contract in 2005.

Tescom Israel has showed a slight increase in revenues over the comparative period in 2005, primarily due to several new large contracts at top-tier customers in the Israeli market. These wins were partially offset by a reduction in activity in the defence sector. The market continues to be very competitive, which is reflected in significantly lower margins. In light of this, we have implemented a cost reduction programme, and have restructured the sales team.

Since the beginning of 2006, we have placed significant emphasis on strengthening our Global Executive Management Team. In January, we welcomed Phil Serlin, who was appointed Vice-President, Finance. Mr Serlin brings extensive experience in financial reporting and regulatory affairs to Tescom, including significant tenures at both the US Securities and Exchange Commission and the international accounting firm of Deloitte.

We are pleased with our progress over the first two quarters of 2006, which is a trend that we wish to continue for the remainder of the year. Current trading continues to be strong and we do not anticipate any significant impact from the current military confrontation in the north of Israel and Lebanon. Tescom had a difficult year in 2005 and I wish to thank our employees for their efforts, which have contributed to a solid performance in the first half of 2006.

Financial Review

Results

Revenues increased by 14.2%, to \$26.8m from \$23.4m in H105, primarily resulting from new contracts in the UK and the Company's contract with the Ministry of Finance in France, as well as a continuing emphasis on improved management of existing customer accounts.

Pre-tax profit amounted to \$1.1m, versus a loss of \$0.1m in H105 (profit of \$1.1m, net of one-off expenses related to the Company's AIM registration in 2005). Despite the significant increase in revenues, H106 gross profit decreased slightly from H105, mainly as a result of increased competition in Israel and the completion of a high-margin contract in Australia in 2005. G&A expenses decreased by \$0.7m in H106, to \$5.7m from \$6.4m in H105. About \$0.3m of this decrease relates to indirect costs associated with the Company's 2005 AIM registration, while \$0.4m of the decrease reflects a continuing emphasis by the Company on a G&A cost reduction programme, which was initiated towards the end of 2005. Sales and marketing expenditure increased slightly during the period, to \$1.6m, from 1.5m in H105.

The Company's results were also negatively impacted by an increase in financial expenses of \$0.1m, due to exchange rate differences between the dollar and the other operating currencies in the various Group locations, as well as increased borrowing costs on its short-term bank debt. The decrease in other expenses of \$1.0m relates to direct costs associated with the AIM registration in 2005 mentioned above.

The Company used \$1.6m in cash for operating activities in H106, versus \$1.12m of cash generated from operations in H105. The reduction in operating cash flows results primarily from an increase in trade receivables, which is mainly due to the Company's increased turnover. The Company's cash balance at 30 June 2006 was \$1.15m, which also reflects the payment of a \$1.0m dividend in January 2006. The Company maintains short-term bank credit lines in both Israel and the UK in the aggregate amount of approximately \$7.0m. \$2.5m had been drawn against these lines as of 30 June 2006.

Share Buyback

The Board of Tescom announced in July 2005 that it had approved a share buyback of its ordinary shares on the open market. In November, the buyback programme was extended to 31 March 2006. The total amount approved for the share repurchase was approximately \$0.6m. From the July approval to 30 June 2006, 229,671 shares were bought back by the Company for a total sum of approximately \$0.3m. These shares are held as treasury shares by the Company.

Dividends

The Company's dividend policy is subject to the future performance of the Company and its funding requirements. The Company declared a total interim dividend of \$1.0m in the fourth quarter of 2005, which was paid in January 2006. In view of the 2005 financial results, the Board decided not to award a final dividend on account of 2005, and has not declared an interim dividend in 2006 in respect of the six months ended 30 June 2006.

Outlook

Tescom has won a number of significant long-term contracts in 2005 and the first half of 2006. These new contracts have positively affected the top line in H106 and this trend is expected to continue throughout the remainder of the year. Competitive pressures, particularly in the Israeli market, continue to affect gross margins and operating profits, although there are signs of improving performance. The Company continues to focus its efforts on increasing gross margins, including assessing the feasibility of staffing certain projects from less costly off-shore locations where suitable. On a quarter to quarter basis, the Company's revenues and profits have improved for each of the last two quarters. The current military confrontation in the north of Israel and in Lebanon is not expected to have a material effect on our revenues and net profits, and we do not anticipate any other adverse effect on our business. We anticipate continuing the progress that has been achieved over the last two quarters, but the Board remains cautious, at this point, in its outlook for the year as a whole.

The Board of Tescom continues to examine a number of strategic opportunities to expand its businesses in other regions and enhance shareholder value.

TESCOM SOFTWARE SYSTEMS TESTING LTD.

CONSOLIDATED BALANCE SHEETS

In thousands of US dollars

	December 31, 2005	June 30, 2006
	Audited	Unaudited
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	2,653	1,145
Trade receivables	11,363	14,702
Other current assets and prepaid expenses	636	766
Total current assets	14,652	16,613
NON-CURRENT ASSETS:		
Severance pay fund	2,155	2,348
Property and equipment, net	1,100	1,291
Deferred income taxes	1,008	1,185
Goodwill and other intangible assets	462	598
Total non-current assets	4,725	5,422
Total assets	19,377	22,035

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

CONSOLIDATED BALANCE SHEETS

In thousands of US dollars

	December 31, 2005	June 30, 2006
	Audited	Unaudited
LIABILITIES AND EQUITY		
CURRENT LIABILITIES:		
Short-term bank credit	1,650	2,545
Trade payables	849	2,205
Other current liabilities and accrued expenses	6,855	7,041
Dividend payable	1,021	-
Total current liabilities	<u>10,375</u>	<u>11,791</u>
LONG-TERM LIABILITIES:		
Accrued severance pay	2,427	2,723
Long-term loan	17	11
Total long-term liabilities	<u>2,444</u>	<u>2,734</u>
EQUITY:		
Issued capital	51	51
Share premium	10,881	11,004
Treasury shares, at cost	(173)	(336)
Foreign currency translation reserve	(1,331)	(1,087)
Accumulated deficit	(2,870)	(2,122)
Total equity	<u>6,558</u>	<u>7,510</u>
Total liabilities and equity	<u><u>19,377</u></u>	<u><u>22,035</u></u>

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

August 16, 2006

Date of approval of the
financial statements

Ofer Albeck
CEO and Chairman of
the Board of Directors

Philip Serlin
Vice President, Finance

TESCOM SOFTWARE SYSTEMS TESTING LTD.

CONSOLIDATED STATEMENTS OF OPERATIONS

In thousands of US dollars, except share and per share data

	Year ended December 31,	Six months ended June 30,	
	2005	2005	2006
	Audited	Unaudited	
Revenues	46,461	23,424	26,760
Cost of revenues	29,649	14,596	18,171
Gross profit	16,812	8,828	8,589
Operating expenses:			
Selling and marketing	2,699	1,514	1,630
General and administrative	13,398	6,396	5,728
Total operating expenses	16,097	7,910	7,358
Operating income	715	918	1,231
Financial income (expenses), net	181	16	(128)
Other expenses, net	(1,035)	(1,032)	(5)
Profit (loss) before taxes on income	(139)	(98)	1,098
Taxes on income	938	485	350
Net profit (loss)	(1,077)	(583)	748
Basic and diluted net earnings (loss) per share	(0.07)	(0.04)	0.05
Weighted average number of shares used for computing basic and diluted net earnings (loss) per share	15,522,414	15,943,099	15,785,768

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

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

In thousands of US dollars

	Share capital	Share premium	Treasury shares, at cost	Foreign currency translation reserve	Equity component of convertible instrument	Accumulated deficit	Total equity
Balance as of January 1, 2005 (audited)	48	8,676	-	(582)	958	(772)	8,328
Share compensation expenses	-	446	-	-	-	-	446
Shares repurchased by the Company	-	-	(173)	-	-	-	(173)
Exercise of options	3	801	-	-	-	-	804
Foreign currency translation adjustments	-	-	-	(749)	-	-	(749)
Repayment of convertible debentures	-	958	-	-	(958)	-	-
Dividends	-	-	-	-	-	(1,021)	(1,021)
Net loss	-	-	-	-	-	(1,077)	(1,077)
Balance as of December 31, 2005 (audited)	51	10,881	(173)	(1,331)	-	(2,870)	6,558
Share compensation expenses	-	123	-	-	-	-	123
Shares repurchased by the Company	-	-	(163)	-	-	-	(163)
Foreign currency translation adjustments	-	-	-	244	-	-	244
Net profit	-	-	-	-	-	748	748
Balance as of June 30, 2006 (unaudited)	51	11,004	(336)	(1,087)	-	(2,122)	7,510

	Share capital	Share premium	Foreign currency translation reserve	Equity component of convertible instrument	Accumulated deficit	Total equity
Balance as of January 1, 2005 (audited)	48	8,676	(582)	958	(772)	8,328
Stock compensation expenses	-	414	-	-	-	414
Exercise of options	3	790	-	-	-	793
Foreign currency translation adjustments	-	-	(438)	-	-	(438)
Repayment of convertible debentures	-	958	-	(958)	-	-
Net loss	-	-	-	-	(583)	(583)
Balance as of June 30, 2005 (unaudited)	51	10,838	(1,020)	-	(1,355)	8,514

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

In thousands of US dollars

	Year ended December 31,	Six months ended June 30,	
	2005	2005	2006
	Audited	Unaudited	
<u>Cash flows from operating activities:</u>			
Net profit (loss)	(1,077)	(583)	748
Adjustments to reconcile net profit (loss) to net cash provided by (used in) operating activities:			
Share compensation expenses	446	414	123
Depreciation and amortization	357	137	275
Loss on impairment of goodwill	945	-	-
Increase in accrued severance pay, net	101	88	90
Exchange differences on convertible debentures	182	147	-
Deferred income taxes, net	(206)	(117)	(144)
Decrease (increase) in trade receivables	(588)	16	(2,774)
Decrease (increase) in other current assets and prepaid expenses	426	265	(331)
Increase in trade payables	122	428	1,057
Increase (decrease) in other current liabilities and accrued expenses	905	443	(166)
Net cash provided by (used in) operating activities	<u>1,613</u>	<u>1,238</u>	<u>(1,122)</u>
<u>Cash flows from investing activities:</u>			
Additions to property and equipment	(979)	(361)	(70)
Proceeds from sale of property and equipment	128	-	8
Proceeds from maturity of short-term bank deposits	<u>1,723</u>	<u>1,760</u>	<u>-</u>
Net cash provided by (used in) investing activities	<u>872</u>	<u>1,399</u>	<u>(62)</u>
<u>Cash flows from financing activities:</u>			
Dividend payment	-	-	(1,021)
Short-term bank credit, net	(300)	(324)	807
Repayment of convertible debentures	(4,500)	(4,500)	-
Exercise of options	804	793	-
Shares repurchased by the Company	(173)	-	(163)
Proceeds from long-term bank loan	40	23	-
Repayment of long-term bank loan	<u>(10)</u>	<u>-</u>	<u>(8)</u>
Net cash used in financing activities	<u>(4,139)</u>	<u>(4,007)</u>	<u>(385)</u>
Effect of exchange rate changes on cash and cash equivalents	<u>(274)</u>	<u>(172)</u>	<u>61</u>
Decrease in cash and cash equivalents	(1,928)	(1,542)	(1,508)
Cash and cash equivalents at the beginning of the period	<u>4,581</u>	<u>4,581</u>	<u>2,653</u>
Cash and cash equivalents at the end of the period	<u><u>2,653</u></u>	<u><u>3,039</u></u>	<u><u>1,145</u></u>

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

TESCOM SOFTWARE SYSTEMS TESTING LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

In thousands of US dollars

	Year ended December 31, 2005	Six months ended June 30,	
	Audited	2005	2006
		Unaudited	
(a) <u>Supplemental disclosure of cash flows:</u>			
Cash paid during the period for:			
Interest	23	52	72
Income taxes	483	433	548
(b) <u>Cash received during the period for interest</u>	55	76	25
(c) <u>Supplemental disclosure of non-cash transactions:</u>			
Dividends declared	1,021	-	-
Property and equipment acquired on credit	-	-	229

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

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

In thousands of US dollars

NOTE 1:- GENERAL

- a. These financial statements have been prepared in a condensed format as of June 30, 2006 and for the six months then ended. These financial statements should be read in conjunction with the audited annual financial statements of the Company as of December 31, 2005, and their accompanying notes.
- b. The interim condensed consolidated financial statements herein have been prepared in accordance with IAS 34, "Interim Financial Reporting", on the historical cost basis. The significant accounting policies and methods of computations applied in the preparation of the interim financial statements are the same as those applied in the annual financial statements as of December 31, 2005. The Group also prepares its consolidated financial statements in accordance with accounting principles generally accepted in Israel ("Israeli GAAP"), pursuant to regulations of the Israel Securities Authority. Under Israeli GAAP, the Group's net profit for the six months ended June 30, 2006 amounted to \$ 853, and total equity as of June 30, 2006 amounted to \$ 7,447, translated from NIS to US dollars, based on the exchange rate on June 30, 2006.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES

Following are data regarding the representative exchange rates of the New Israeli Shekel ("NIS") and the Pound Sterling in relation to the US dollar:

<u>As of</u>	<u>Exchange rate of one US dollar</u>	<u>Exchange rate of one Pound Sterling</u>
June 30, 2006	NIS 4.440	NIS 8.138
June 30, 2005	NIS 4.574	NIS 8.197
December 31, 2005	NIS 4.603	NIS 7.940

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**In thousands of US dollars, except share data****NOTE 3:- SEGMENT INFORMATION***Six months ended June 30, 2006 (unaudited):*

	<u>North America</u>	<u>Europe</u>	<u>Israel</u>	<u>Other</u>	<u>Total</u>
Segment revenues	<u>2,556</u>	<u>13,747</u>	<u>8,834</u>	<u>1,623</u>	<u>26,760</u>
Segment results	<u>5</u>	<u>1,723</u>	<u>(717)</u>	<u>220</u>	<u>1,231</u>

Six months ended June 30, 2005 (unaudited):

	<u>North America</u>	<u>Europe</u>	<u>Israel</u>	<u>Other</u>	<u>Total</u>
Segment revenues	<u>2,670</u>	<u>10,771</u>	<u>8,743</u>	<u>1,240</u>	<u>23,424</u>
Segment results	<u>421</u>	<u>921</u>	<u>(720)</u>	<u>296</u>	<u>918</u>

Year ended December 31, 2005 (audited):

	<u>North America</u>	<u>Europe</u>	<u>Israel</u>	<u>Other</u>	<u>Total</u>
Revenues:					
Segment revenues	5,341	21,530	16,678	2,918	46,467
Inter-segment sales			(6)		(6)
Sales to external customers	<u>5,341</u>	<u>21,530</u>	<u>16,672</u>	<u>2,918</u>	<u>46,461</u>
Segment results	<u>(881)</u>	<u>2,348</u>	<u>(1,665)</u>	<u>913</u>	<u>715</u>

NOTE 4:- OTHER EVENTS DURING THE REPORTING PERIOD

During the period, the Company repurchased 116,345 treasury shares for aggregate consideration of \$ 163.