



March 14, 2007

Israeli Technology

Stock Rating:
Sector Performer

Sector Weighting:
Market Weight

12-18 mo. Price Target	\$36.00
ESLT-OTC (3/14/07)	\$33.60

Key Indices: NASDAQ

3-5-Yr. EPS Gr. Rate (E)	10.0%
52-week Range	\$23.01-\$36.01
Shares Outstanding	41.9M
Float	12.0M Shrs
Avg. Daily Trading Vol.	10,000
Market Capitalization	\$1,408.3M
Dividend/Div Yield	\$0.60 / 1.8%
Fiscal Year Ends	December
Book Value	\$11.41 per Shr
2007 ROE (E)	13.5%
LT Debt	\$171.8M
Preferred	Nil
Common Equity	\$478.4M
Convertible Available	No

Earnings per Share	Prev	Current
2005		\$1.22A
2006	\$1.76E	\$1.78A
2007	\$1.98E	\$2.00E

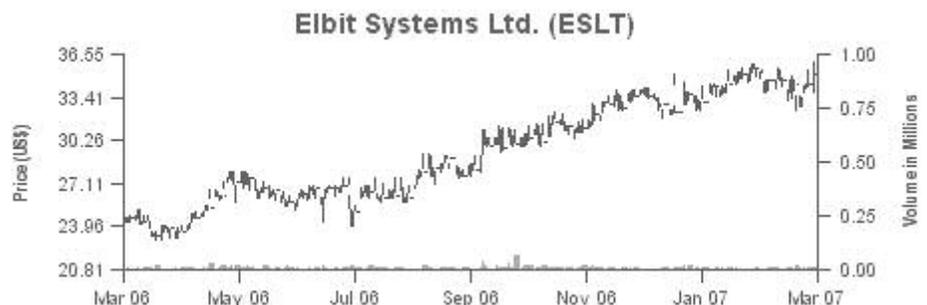
P/E		
2005		27.5x
2006	19.1x	18.9x
2007	17.0x	16.8x

Elbit Systems Ltd.

Strong Finish to Record Year; Expect More of the Same Next Year

- Elbit wrapped up FY06 with record revenue and backlog driven by strong sales in Land Systems and Electro-Optical products. The company is likely to continue growing through FY07 with demand for its products propelled by a wide variety of military and homeland security needs.
- 4Q06 sales of \$467M (up 45.3% YoY) beat our \$399 million and the Street's \$388M target. EPS of \$0.57 beat our \$0.55 and the Street's \$0.50. Earnings would have been stronger if not for Elisra, whose weak gross margins were the one disappointment.
- We are adjusting estimates to reflect Elbit's top-line growth and strong momentum across several geographies and product lines. Our FY07 revenue moves to \$1.64B from \$1.57B and EPS to \$2.00 from \$1.98.
- We are nudging our PT to \$36 from \$35. Our PT is achieved by applying an 18x multiple to our FY07E EPS of \$2.00. The target multiple is in the middle of peers' 15x-20x range and is supported by record backlog levels, increased visibility into FY07 and the likelihood of further upward revisions.

Stock Price Performance



Source: Reuters

All figures in US dollars, unless otherwise stated.

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Company Description

Elbit is a defense electronics company focused on electro optics, communications, UAV and upgrade programs.

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See "Price Target Calculation" and "Key Risks to Price Target" sections at the end of this report, where applicable.

Strong 4Q06 Sets Stage for FY07

Elbit's fourth-quarter revenue of \$467M grew 24.1% sequentially (all organic) and 45.3% YoY, with the key drivers—Land Systems and Electro-Optical products—providing solid momentum into FY07.

We are equally encouraged by Elbit's record backlog of \$3.8 billion, which grew by an impressive 13.1% from 4Q05. We believe that the company will continue to grow its backlog through FY07. The company also mentioned that it has an estimated \$1 billion in "soft-backlog" (orders not yet funded).

The exceptional visibility, together with a strong pipeline of meaningful growth opportunities, including in the U.S. with the Secure Border project and with NATO, leave us upbeat about the possibilities in FY07.

Elisra, where slower than expected rationalization was the one disappointment during 4Q, could continue to create some drag on profitability through FY07. We believe it will take at least another year for Elisra to become earnings neutral.

Impressive 4Q06

Fourth-quarter record revenues of \$467M showed impressive growth of 24.1% QoQ and 45.3% YoY, outpacing our revenue estimate of \$399 million and consensus estimate of \$388 million. The upside was driven by an increase in revenue from Land Systems sales to the U.S. Marine Corps, strong growth in its Electro-Optical business and the U.K. Watchkeeper project.

On the bottom line, EPS of \$0.57 beat our target of \$0.55 and was well above consensus estimate of \$0.50. Gross margin of 21.4% was lower due to the slower than expected rationalization of Elisra.

Record High Visibility

Elbit's backlog grew 0.4% sequentially to reach a new high of \$3.79 billion, with 70% of backlog expected to turn into revenue between FY07 and FY08.

Helping drive the backlog increases were a number of additional contracts, including: a \$51 million deal to supply the Helmet Display and Tracking System for the U.S. Army and a \$58 million order to the Belgian Infantry Vehicle Program to supply unmanned turrets and electro-optic systems.

We expect backlog to continue growing in FY07, with the U.S. SBInet project and the European business likely to be key drivers. In Europe we are encouraged by Elbit's win with the German Air Force for personal survival radios, a deal that could open the gate to meaningful orders from NATO next year.

The Bulgarian Ministry of Defense terminated a €57M (approximately US \$75.5M) order for the modernization of Mi-24 and Mi-17 helicopters. We do not expect that this to have a material adverse effect on the company's operations.

Strong Growth in U.S. & Europe and Land Systems

In terms of geographic distribution in 4Q06, U.S. and Europe revenues had the strongest YoY growth: U.S. and Europe grew a remarkable 98.5% and 99.5% respectively. Revenues in other geographies increased by 27.6% and Israel fell by 13.7%.

4Q06 also showed solid YoY growth in most product areas. Land systems were exceptionally strong, growing 524% YoY. This largely reflects systems supplied to the U.S. Marine Corps.

Airborne Systems accounted for a healthy 27.9% of revenues (34.6% in 4Q05), Land systems for 25.2% (5.9% in 4Q05), C4ISR for 20.4% (26.1% in 4Q05) Electro-Optical for 20.1% (27.5% in 4Q05) and other for 6.1% (5.9% in 4Q05).

Elisra May Turn at End of FY07

The company expects Elisra's effect on the bottom line to turn neutral or become slightly positive in 4Q07 or 1Q08. For FY06, Elisra's revenues were \$219M, gross profit \$29M and net loss \$26M. Elbit's share of net loss was \$18M (70%).

Elbit has adopted an efficiency plan that includes a reduction in employee headcount, consolidating operating sites and streamlining operations.

Adjusting Estimates

We are increasing our estimates to reflect Elbit's solid top-line growth. Better progress at Elisra could potentially lead to gross margin expansion and upward revisions on the bottom line.

- For 1Q07, we are introducing revenue estimates of \$397 million and EPS of \$0.45.
- We are increasing our FY07 estimates to \$1.64 billion in revenue and \$2.00 in EPS from \$1.57 billion and \$1.98 respectively.

We highlight that the complex staging and revenue recognition structure of most of Elbit's projects increases the likelihood of quarter-to-quarter fluctuations. Our focus is on full-year results, however, where Elbit's backlog coverage provides us with a high degree of confidence that current estimates will be met or exceeded.

Price Target Calculation

We are nudging our price target to \$36 from \$35. Our price target is achieved by applying a multiple of 18x to our FY07E EPS of \$2.00. Our 18x target multiple is near the middle of the peer group's range of 15x-20x, reflecting Elbit's faster than industry average top- and bottom-line growth. We believe that record backlog levels further support this multiple and our price target. New momentum in unmanned systems sales following the Watchkeeper win coupled with solid execution of Elbit's consolidation plans could support further upward estimate revisions in 2007, in our view. Expansion of the U.S. "SBIInet Project," Boeing and momentum in Europe could also lead to upward revisions.

Key Risks to Price Target

Potential risks to our price target include slow demand for platform upgrades, decreasing budgets for defense spending (in Israel and elsewhere), political risk pertaining to Israel's relationship with customer countries and execution risks related to Elbit's ongoing consolidation of the Israeli defense sector and international M&A plans.

Exhibit 1.**Elbit Systems Ltd.**

(\$ and Shares in '000, Except Per Share Figures)

	FY 2005A	Quarter Ending				FY 2006A	Quarter Ending				FY 2007E
		Mar-06A	Jun-06A	Sep-06A	Dec-06A		Mar-07E	Jun-07E	Sep-07E	Dec-07E	
Revenues	\$1,069,876	\$334,370	\$344,815	\$376,670	\$467,388	\$1,523,243	\$397,280	\$405,225	\$413,330	\$421,183	\$1,637,018
Cost of revenue	786,616	246,830	255,237	280,538	367,163	1,149,768	295,973	300,677	305,037	309,570	1,211,258
Gross profit	\$283,260	\$87,540	\$89,578	\$96,132	\$100,225	\$373,475	\$101,306	\$104,548	\$108,292	\$111,614	\$425,760
Research & Development	71,903	21,438	18,351	24,574	27,869	92,232	26,220	26,745	26,866	27,377	107,209
Sales & Marketing	78,648	26,248	27,382	27,397	30,853	111,880	29,796	30,797	31,826	32,010	124,429
General & Administrative	54,697	19,007	18,720	19,727	20,051	77,505	20,261	20,788	21,080	21,480	83,609
Total Operating Expenses	\$205,248	\$66,693	\$64,453	\$71,698	\$78,773	\$281,617	\$76,278	\$78,330	\$79,773	\$80,867	\$315,248
Operating Income	\$78,012	\$20,847	\$25,125	\$24,434	\$21,452	\$91,858	\$25,029	\$26,218	\$28,520	\$30,746	\$110,513
Interest Income (Expense)	(11,473)	(4,241)	(6,677)	(4,445)	(6,093)	(21,456)	(6,100)	(6,100)	(6,100)	(6,100)	(24,400)
Other Income (Expense)	(5,046)	908	(748)	231	1,423	1,814	100	110	120	150	480
Pre-tax income	\$61,493	\$17,514	\$17,700	\$20,220	\$16,782	\$72,216	\$19,029	\$20,228	\$22,540	\$24,796	\$86,593
Income Taxes (Benefit)	16,335	4,604	4,762	7,279	4,049	20,694	4,947	5,259	5,860	6,447	22,514
Minority Interest and Equity Losses	5,750	1,558	4,333	5,802	11,227	22,920	5,000	5,000	5,000	5,000	20,000
Net Income	\$50,908	\$14,468	\$17,271	\$18,743	\$23,960	\$74,442	\$19,081	\$19,969	\$21,679	\$23,349	\$84,079
Diluted EPS	\$1.22	\$0.35	\$0.41	\$0.45	\$0.57	\$1.78	\$0.45	\$0.47	\$0.51	\$0.55	\$2.00
WA Shares Outstanding	41,623	41,736	41,808	41,913	41,955	41,853	41,937	42,063	42,189	42,315	42,126

Source: Company data, CIBC World Markets estimates

Exhibit 2.**Elbit Systems Ltd.**

Margin Analysis	FY	Quarter Ending				FY	Quarter Ending				FY
	2005A	Mar-06A	Jun-06A	Sep-06A	Dec-06A	2006A	Mar-07E	Jun-07E	Sep-07E	Dec-07E	2007E
Gross margin	26.5%	26.2%	26.0%	25.5%	21.4%	24.5%	25.5%	25.8%	26.2%	26.5%	26.0%
Research & Development	6.7%	6.4%	5.3%	6.5%	6.0%	6.1%	6.6%	6.6%	6.5%	6.5%	6.5%
Sales & Marketing	7.4%	7.8%	7.9%	7.3%	6.6%	7.3%	7.5%	7.6%	7.7%	7.6%	7.6%
General & Administrative	5.1%	5.7%	5.4%	5.2%	4.3%	5.1%	5.1%	5.1%	5.1%	5.1%	5.1%
Operating Margin	7.3%	6.2%	7.3%	6.5%	4.6%	6.0%	6.3%	6.5%	6.9%	7.3%	6.8%
Pre-Tax Margin	5.7%	5.2%	5.1%	5.4%	3.6%	4.7%	4.8%	5.0%	5.5%	5.9%	5.3%
Effective Tax Rate	26.6%	26.3%	26.9%	36.0%	24.1%	28.7%	26.0%	26.0%	26.0%	26.0%	26.0%
Net Income Margin	4.8%	4.3%	5.0%	5.0%	5.1%	4.9%	4.8%	4.9%	5.2%	5.5%	5.1%
Sequential Growth Rates											
Revenues		3.9%	3.1%	9.2%	24.1%		-15.0%	2.0%	2.0%	1.9%	
Research & Development		16.1%	-14.4%	33.9%	13.4%		-5.9%	2.0%	0.5%	1.9%	
Sales & Marketing		9.6%	4.3%	0.1%	12.6%		-3.4%	3.4%	3.3%	0.6%	
General & Administrative		17.7%	-1.5%	5.4%	1.6%		1.0%	2.6%	1.4%	1.9%	
Year-on-year Growth Rates											
Revenue	13.8%	44.9%	41.4%	37.6%	45.3%	42.4%	18.8%	17.5%	9.7%	-9.9%	7.5%
Gross Profit	13.5%	42.2%	35.5%	30.5%	22.3%	31.8%	15.7%	16.7%	12.6%	11.4%	14.0%
Operating Income	21.2%	22.8%	42.6%	21.9%	-8.2%	17.7%	20.1%	4.4%	16.7%	43.3%	20.3%
Pre-tax Income	3.7%	13.6%	10.1%	19.2%	28.8%	17.4%	8.6%	14.3%	11.5%	47.8%	19.9%
Net Income	-2.0%	10.1%	19.9%	18.9%	215.1%	46.2%	31.9%	15.6%	15.7%	-2.5%	12.9%
WA Shares Outstanding	1.1%	0.2%	0.4%	0.4%	0.4%	0.6%	0.2%	0.3%	0.3%	0.3%	0.7%
Diluted EPS	-3.4%	9.8%	19.4%	18.0%	212.9%	45.4%	31.3%	14.9%	14.9%	-3.4%	12.2%

Source: Company data, CIBC World Markets estimates

Our EPS estimates are shown below:

	1 Qtr.	2 Qtr.	3 Qtr.	4 Qtr.	Yearly
2005 Current	\$0.32A	\$0.35A	\$0.38A	\$0.18A	\$1.22A
2006 Prior	\$0.35A	\$0.41A	\$0.45A	\$0.55E	\$1.76E
2006 Current	\$0.35A	\$0.41A	\$0.45A	\$0.57A	\$1.78A
2007 Prior	--	--	--	--	\$1.98E
2007 Current	\$0.45E	\$0.47E	\$0.51E	\$0.55E	\$2.00E

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CIBC World Markets Price Chart



HISTORICAL PERFORMANCE OF CIBC WORLD MARKETS' RECOMMENDATIONS FOR ELBIT SYSTEMS LTD. (ESLT)

Date	Change Type	Closing Price	Rating	Price Target	Coverage
08/04/2004	▲	20.70	SP	23.00	Shaul Eyal
11/19/2004	▲	22.67	SP	25.00	Shaul Eyal
01/11/2005	▲	25.31	SP	28.00	Shaul Eyal
05/18/2006	▲	27.12	SP	30.00	Shaul Eyal
11/15/2006	▲	31.43	SP	35.00	Shaul Eyal

CIBC World Markets' Stock Rating System

Abbreviation	Rating	Description
Stock Ratings		
SO	Sector Outperformer	Stock is expected to outperform the sector during the next 12-18 months.
SP	Sector Performer	Stock is expected to perform in line with the sector during the next 12-18 months.
SU	Sector Underperformer	Stock is expected to underperform the sector during the next 12-18 months.
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R	Restricted	CIBC World Markets is restricted*** from rating the stock.
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O	Overweight	Sector is expected to outperform the broader market averages.
M	Market Weight	Sector is expected to equal the performance of the broader market averages.
U	Underweight	Sector is expected to underperform the broader market averages.
NA	None	Sector rating is not applicable.

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Sector Outperformer (Buy)	340	39.0%	Sector Outperformer (Buy)	182	53.5%
Sector Performer (Hold/Neutral)	429	49.3%	Sector Performer (Hold/Neutral)	220	51.3%
Sector Underperformer (Sell)	72	8.3%	Sector Underperformer (Sell)	36	50.0%
Restricted	18	2.1%	Restricted	18	100.0%

Ratings Distribution: Israeli Technology Coverage Universe

(as of 14 Mar 2007)	Count	Percent	Inv. Banking Relationships	Count	Percent
Sector Outperformer (Buy)	3	37.5%	Sector Outperformer (Buy)	1	33.3%
Sector Performer (Hold/Neutral)	5	62.5%	Sector Performer (Hold/Neutral)	2	40.0%
Sector Underperformer (Sell)	0	0.0%	Sector Underperformer (Sell)	0	0.0%
Restricted	0	0.0%	Restricted	0	0.0%

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