

**TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES  
UNAUDITED CONDENSED INTERIM  
CONSOLIDATED FINANCIAL STATEMENTS  
AS OF JUNE 30, 2012**

**TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES**

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CONSOLIDATED FINANCIAL STATEMENTS  
AS OF JUNE 30, 2012**

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**TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES**  
**UNAUDITED CONDENSED INTERIM**  
**CONSOLIDATED BALANCE SHEETS**  
(dollars in thousands)

	<u>As of</u> <u>June 30,</u>	<u>As of</u> <u>December 31,</u>
	<u>2012</u>	<u>2011</u>
	<u>(unaudited)</u>	
<b>A S S E T S</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 139,089	\$ 101,149
Interest bearing deposits	31,572	--
Trade accounts receivable	91,928	75,350
Other receivables	6,783	5,000
Inventories	64,294	69,024
Other current assets	<u>14,716</u>	<u>15,567</u>
Total current assets	<u>348,382</u>	<u>266,090</u>
<b>LONG-TERM INVESTMENTS</b>	<u>12,555</u>	<u>12,644</u>
<b>PROPERTY AND EQUIPMENT, NET</b>	<u>472,592</u>	<u>498,683</u>
<b>INTANGIBLE ASSETS, NET</b>	<u>52,620</u>	<u>58,737</u>
<b>GOODWILL</b>	<u>7,000</u>	<u>7,000</u>
<b>OTHER ASSETS, NET</b>	<u>14,715</u>	<u>14,067</u>
<b>TOTAL ASSETS</b>	<b>\$ <u>907,864</u></b>	<b>\$ <u>857,221</u></b>
 <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES</b>		
Current maturities of debentures and short-term bank debt	\$ 41,619	\$ 48,255
Trade accounts payable	96,743	111,620
Deferred revenue and short-term customers' advances	4,835	5,731
Other current liabilities	<u>66,608</u>	<u>64,654</u>
Total current liabilities	<u>209,805</u>	<u>230,260</u>
<b>LONG-TERM LOANS FROM BANKS</b>	124,959	103,845
<b>DEBENTURES</b>	277,275	197,765
<b>LONG-TERM CUSTOMERS' ADVANCES</b>	7,447	7,941
<b>EMPLOYEES RELATED LIABILITES</b>	87,149	97,927
<b>DEFERRED TAX LIABILITY</b>	25,782	20,428
<b>OTHER LONG-TERM LIABILITIES</b>	<u>23,721</u>	<u>24,352</u>
Total liabilities	<u>756,138</u>	<u>682,518</u>
<b>SHAREHOLDERS' EQUITY</b>	<u>151,726</u>	<u>174,703</u>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>	<b>\$ <u>907,864</u></b>	<b>\$ <u>857,221</u></b>

See notes to consolidated financial statements.

**TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES**  
**UNAUDITED CONDENSED INTERIM**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(dollars in thousands, except per share data)

	Six months ended June 30,		Three months ended June 30,	
	2012	2011	2012	2011
	(unaudited)		(unaudited)	
<b>REVENUES</b>	\$ 336,650	\$ 260,327	\$ 168,637	\$ 139,707
<b>COST OF REVENUES</b>	<u>285,564</u>	<u>209,408</u>	<u>140,299</u>	<u>119,333</u>
<b>GROSS PROFIT</b>	<u>51,086</u>	<u>50,919</u>	<u>28,338</u>	<u>20,374</u>
<b>OPERATING COSTS AND EXPENSES</b>				
Research and development	15,582	11,081	7,582	5,457
Marketing, general and administrative	22,195	20,517	9,695	10,948
Acquisition related and reorganization costs	<u>5,789</u>	<u>1,493</u>	<u>5,789</u>	<u>1,493</u>
	<u>43,566</u>	<u>33,091</u>	<u>23,066</u>	<u>17,898</u>
<b>OPERATING PROFIT</b>	7,520	17,828	5,272	2,476
<b>FINANCING EXPENSE, NET</b>	(27,238)	(29,713)	(8,709)	(10,499)
<b>GAIN FROM ACQUISITION</b>	--	19,467	--	19,467
<b>OTHER EXPENSE, NET</b>	<u>(1,019)</u>	<u>(404)</u>	<u>(1,019)</u>	<u>(319)</u>
<b>PROFIT (LOSS) BEFORE INCOME TAX</b>	(20,737)	7,178	(4,456)	11,125
<b>INCOME TAX EXPENSE</b>	<u>(7,984)</u>	<u>(10,846)</u>	<u>(4,948)</u>	<u>(9,382)</u>
<b>NET PROFIT (LOSS) FOR THE PERIOD</b>	<u>\$ (28,721)</u>	<u>\$ (3,668)</u>	<u>\$ (9,404)</u>	<u>\$ 1,743</u>
<b>BASIC EARNING (LOSS) PER ORDINARY SHARE (*)</b>	<u>\$ (1.34)</u>	<u>\$ (0.19)</u>	<u>\$ (0.44)</u>	<u>\$ 0.09</u>
<b>DILUTED EARNING (LOSS) PER ORDINARY SHARE (*)</b>	<u>\$ (1.34)</u>	<u>\$ (0.19)</u>	<u>\$ (0.44)</u>	<u>\$ 0.03</u>

(\*) Earning (Loss) per ordinary share includes the effect of the reverse stock split of one-for-fifteen effected on August 5, 2012.

See notes to consolidated financial statements.

**TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES**  
**UNAUDITED CONDENSED INTERIM**  
**CONSOLIDATED COMPREHENSIVE INCOME (LOSS)**  
(dollars in thousands)

	Three months ended		Six months ended	
	June 30,		June 30,	
	2012	2011	2012	2011
	<u>(unaudited)</u>		<u>(unaudited)</u>	
<b>Income (loss) for the period</b>	\$ (9,404)	\$ 1,743	\$ (28,721)	\$ (3,668)
<b>Foreign currency translation adjustment</b>	3,029	624	(2,668)	624
<b>Other comprehensive loss</b>	(933)	(755)	(369)	(1,116)
<b>Comprehensive income (loss) for the period</b>	<u>\$ (7,308)</u>	<u>\$ 1,612</u>	<u>\$ (31,758)</u>	<u>\$ (4,160)</u>

**TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES**  
**UNAUDITED CONDENSED INTERIM**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(dollars in thousands)

	Six months ended	
	June 30,	
	2012	2011
	<u>(unaudited)</u>	
<b>CASH FLOWS - OPERATING ACTIVITIES</b>		
Net Loss for the period	\$ (28,721)	\$ (3,668)
Adjustments to reconcile net loss for the period to net cash provided by operating activities:		
Income and expense items not involving cash flows:		
Depreciation and amortization	84,464	66,707
Effect of indexation, translation and fair value measurement on debt	6,730	6,536
Other expense (income), net	1,019	(1,973)
Gain from acquisition	--	(19,467)
Changes in assets and liabilities:		
Trade accounts receivable	(17,430)	(22,759)
Other receivables and other current assets	(2,958)	(2,911)
Inventories	4,273	(7,122)
Trade accounts payable	3,367	27,079
Deferred revenue and customers' advances	(1,390)	(18,597)
Other current liabilities	1,294	13,977
Deferred tax liability, net	7,776	--
Other long-term liabilities	334	(1,697)
	<u>58,758</u>	<u>36,105</u>
Reorganization – retirement plan	(8,851)	--
Net cash provided by operating activities	<u>49,907</u>	<u>36,105</u>
<b>CASH FLOWS - INVESTING ACTIVITIES</b>		
Investments in property and equipment	(51,334)	(56,266)
Proceeds related to sale and disposal of property and equipment	--	5,751
Investments in other assets, intangible assets and others	(4,369)	--
Acquisition of subsidiary consolidated for the first time (a)	--	(40,000)
Interest bearing deposits, including designated deposits	(31,572)	35,507
Net cash used in investing activities	<u>(87,275)</u>	<u>(55,008)</u>
<b>CASH FLOWS - FINANCING ACTIVITIES</b>		
Proceeds on account of shareholders' equity	78,913	20,617
Proceeds from long-term loans	14,443	--
Short-term bank debt	3,800	--
Debts repayment	(21,314)	(25,744)
Net cash provided by (used in) financing activities	<u>75,842</u>	<u>(5,127)</u>
Effect of foreign exchange rate change	<u>(534)</u>	<u>71</u>
<b>INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>37,940</b>	<b>(23,959)</b>
<b>CASH AND CASH EQUIVALENTS - BEGINNING OF PERIOD</b>	<b><u>101,149</u></b>	<b><u>100,375</u></b>
<b>CASH AND CASH EQUIVALENTS - END OF PERIOD</b>	<b>\$ <u>139,089</u></b>	<b>\$ <u>76,416</u></b>

**TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(dollars in thousands)

	Six months ended June 30,	
	2012	2011
	(unaudited)	
<b>NON-CASH ACTIVITIES</b>		
Investments in property and equipment	\$ 16,033	\$ 15,595
Conversion of convertible debentures to share capital and exercise of warrant	\$ --	\$ 7,006
Shares issued to the Banks in consideration for the interest reduction, following September 2006 amendment with the Banks	\$ --	\$ 12,087
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>		
Cash paid during the period for interest	\$ 18,620	\$ 14,539
Cash paid during the period for income taxes	\$ (1,085)	\$ 3,416
 <b>(a) ACQUISITION OF SUBSIDIARY :</b>		
Assets and liabilities of the subsidiary as of June 2, 2011:		
Working capital (excluding cash and cash equivalents)		\$ (2,534)
Property, plant, and equipment, including real estate		145,559
Intangible assets		11,156
Other assets		2,900
Long-term liabilities		(74,984)
		82,097
Less :		
Issuance of share capital		22,630
Gain from acquisition		19,467
		42,097
Cash paid for the acquisition of a subsidiary		\$ 40,000

See notes to consolidated financial statements.

**TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED INTERIM CONSOLIDATED**  
**FINANCIAL STATEMENTS AS OF JUNE 30, 2012**  
(dollars in thousands, except share data and per share data)

**NOTE 1 - GENERAL**

**A. Basis for Presentation**

- (1) The condensed interim consolidated financial statements of Tower Semiconductor Ltd. (“Tower”) include the financial statements of Tower and its wholly-owned subsidiaries (i) Jazz Technologies, Inc. and its wholly-owned subsidiary, Jazz Semiconductor, Inc, an independent semiconductor foundry focused on specialty process technologies for the manufacture of analog intensive mixed-signal semiconductor devices (Jazz Technologies, Inc. and its wholly-owned subsidiaries are collectively referred to herein as “Jazz”), and (ii) from June 2011, TowerJazz Japan Ltd. (“TJP”), a company which owns and operates the facility acquired in Nishiwaki, Japan. Tower and its wholly-owned subsidiaries are referred to as the “Company”. References to the “Company” for dates prior to the acquisition of TJP do not include TJP.
- (2) The interim consolidated financial statements are presented in accordance with U.S. generally accepted accounting principles (“US GAAP”).

The Company’s consolidated financial statements include TJP results as from June 3, 2011. The Company’s consolidated financial statements are presented after elimination of inter-company transactions and balances. The unaudited condensed interim consolidated financial statements as of June 30, 2012 of the Company should be read in conjunction with the audited consolidated financial statements of the Company as of December 31, 2011 and for the year then ended, including the notes thereto.

In the opinion of management, the interim financial statements include all adjustments necessary for a fair presentation of the financial position and results of operations as of the date and for the interim periods presented. The results of operations for the interim periods are not necessarily indicative of the results to be expected on a full-year basis.

- (3) Certain amounts in prior periods’ financial statements have been reclassified in order to conform to the 2012 presentation.

**TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED INTERIM CONSOLIDATED**  
**FINANCIAL STATEMENTS AS OF JUNE 30, 2012**  
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**NOTE 1 - GENERAL (cont.)**

**B. Financing of the Company's Debt Obligations and Other Liabilities**

During the past years, the Company experienced business and financial improvement, as reflected by the improvement in the Company's revenue and margins as compared to the period prior to mid-2009 which was negatively affected by the global economic downturn that commenced in 2008. However, following the recent economic slowdown in Europe and worldwide and following the conditions in the financial markets, the semiconductor industry experienced weakening customer demand and reduced rate of growth.

Market analysts are currently cautious with respect to the global economic conditions forecasted for 2012 and beyond, and there can be no assurance that global economic conditions will not negatively affect the Company's business and financial position. There is no assurance that another downturn in the semiconductor industry and/or in the global economy will not occur. The effects of another downturn in the semiconductor industry and/or in the global economy may include global decreased demand, downward price pressure, excess inventory and unutilized capacity worldwide, which may negatively impact consumer and customer demand for the Company's products and the end products of the Company's customers. A downturn in the semiconductor industry and/or in the global economy may adversely affect the Company's commercial relationships with its customers, suppliers, and creditors, including its lenders, its plans to continue its capacity growth, and the Company's future financial results and position, including its ability to raise funds in the capital markets and to fulfill its debt obligations and other liabilities, comprised mainly of banks' loans and debentures.

The Company is exploring various ways to fund its capacity growth plans and the ramp-up of its business technology capabilities and manufacturing capacity and capabilities, and to fulfill its debt obligations and other liabilities. However there is no assurance as to the extent of such funding or when, if at all, such funding will be available to the Company. Such funding may include, among others, debt restructuring and/or refinancing, possible financing transactions, sale of assets, intellectual property licensing, possible sale and lease-back of real estate assets and improving cash flow from operations thorough operating efficiencies.

See further details in Notes 3, 7B, 12B, 13, 17 to the 2011 audited consolidated financial statements and Note 2 below.

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**NOTE 2 - RECENT DEVELOPMENTS**

**A. Shares Reverse Split**

In August 2012, Tower completed a reverse split of its ordinary shares at a ratio of 1 for 15 following shareholders approval, to regain compliance with the NASDAQ minimum bid requirement of \$1 per share and maintain Tower's stock listing on NASDAQ. The reverse split reduced the number of outstanding ordinary shares of Tower to approximately 22 million shares. Proportional adjustments were made to all of Tower's outstanding convertible securities such that the underlying shares will be reduced by the ratio of 1 for 15. All amount of shares and other securities of the Company in these financial statements reflect the effect of the reverse stock split.

**B. GE Credit Line Agreement**

In May 2012, TJP signed a definitive credit line agreement with GE Capital to provide a three-year secured asset-based revolving credit line of up to 4 billion Japanese Yen (approximately \$50,000). The borrowing availability varies based on the levels of TJP's eligible accounts receivable, eligible equipment and real estate and other terms and conditions stipulated in the credit line agreement. Loans to be obtained under this credit line will carry an interest of the higher of TIBOR rate or LIBOR rate plus 2.6% per annum. The TJP credit line agreement contains customary covenants and other terms, as well as customary events of default. The facility is secured by a first priority security interest over the assets of TJP. As of June 30, 2012, TJP was in full compliance with all of the covenants under this credit line agreement. Availability under the credit line is calculated according to certain formulas set forth in the agreement and is capped at \$30,000 until June 2013 and \$50,000 thereafter.

As of June 30, 2012 the total availability amounted to \$30,000, of which an amount of approximately \$14,400 was drawdown and unutilized availability amounted to \$15,600.

In connection with the GE credit line agreement, Micron's security interest over the assets of TJP was changed to a second priority security interest, subordinated to GE Capital's first priority security interest. Additionally, Tower, TJP, Micron Technology Inc. and Micron Japan Ltd. entered into an intercreditor agreement governing the subordination and priority of claims over TJP's assets, and the order of priority in the realization of any security interests over TJP's assets.

**TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED INTERIM CONSOLIDATED**  
**FINANCIAL STATEMENTS AS OF JUNE 30, 2012**  
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**NOTE 2 - RECENT DEVELOPMENTS (Cont.)**

**C. Income Tax Audit**

In February 2012, the U.S. tax authorities commenced an audit of Jazz's tax returns, and required certain reports and data in connection with the tax returns of Jazz for these years. There is no indication to date whether Jazz will be required to pay any additional taxes pursuant to this audit.

**D. Registration Statement on Form F-3**

In May 2012 Tower filed a registration statement on Form F-3 with the U.S. Securities and Exchange Commission to register approximately 5.7 million ordinary shares underlying equity equivalent convertible capital notes held by the Banks. The registration statement on Form F-3 has been declared effective by the SEC in July 2012.

**E. February 2012 Debentures Issuance**

In February 2012, Tower raised a net amount of approximately \$80,000 through the expansion of its long-term outstanding debentures Series F. The debentures are US dollar linked, due in two equal installments in December 2015 and December 2016, carry an interest rate of 7.8% per annum, and all its other terms are identical to the Company's existing Series F terms issued in October 2010. In addition, Tower issued warrants exercisable from March 2014 to March 2016 to approximately 1.8 million shares at an exercise price to be determined in February 2014 based on 120% of the then prevailing Company's stock trading price.

**F. Shareholder Equity**

As of the date of the approval of the financial statements, the number of Tower's authorized registered ordinary shares amounts to 120 million.

The weighted average number of ordinary shares outstanding, that was used for the basic earnings (loss) per share calculation, for the six months ended June 30, 2012 and June 30, 2011 was approximately 21.4 million and 19.1 million, respectively, and for the three months ended June 30, 2012 and June 30, 2011 was approximately 21.5 million and 19.7 million, respectively.

The weighted average number of ordinary shares that was used for the diluted earnings per share calculation for the three months ended June 30, 2011 was approximately 47.7 million and the net profit that was used for the diluted earnings per share calculation was \$1,243. According to GAAP, the diluted loss per share for the six months ended June 30, 2012 and 2011 and for the three months ended June 30, 2012 is not to be presented or calculated due to the losses incurred in these periods.