

DIRECTORS REPORT ON THE STATE OF THE COMPANY'S AFFAIRS
FOR THE PERIOD ENDED JUNE 30, 2007

Following is the Directors' Report of Israel Chemicals Ltd. (ICL or the Company) for the period ended June 30, 2007.

1. Description of the Company and its business environment

1.1 Description of ICL

Israel Chemicals (the Company or ICL) is a multinational company that operates mainly in the areas of fertilizers and specialty chemicals, in three segments – fertilizers, industrial products and performance products.

ICL's operations are based primarily on natural resources – potash, bromine, magnesium and sodium chloride from the Dead Sea, and phosphate rock from the Negev Desert, all on the basis of concessions and licenses from the State of Israel. Operations are also based on potash and salt mines in England and Spain under leases and licenses from the competent authorities in those countries. ICL is active in the production of these minerals, in their sale throughout the world, and also in the development, manufacture and marketing of downstream products based primarily on these raw materials.

ICL has a key position in the potash, bromine and purified phosphoric acid and specialty phosphate markets. Potash is a core component of fertilizers. Bromine serves a wide range of applications, primarily in flame retardants. ICL's products are used mainly in agriculture, electronics, food products, oil and gas drilling, water purification and desalination, and in the detergent, paper, cosmetics, pharmaceutical, automotive and aluminum and other industries. ICL has decades of accumulated experience in most of its businesses.

ICL has direct access to most of the raw materials required for its activities, at low cost and high quality, by virtue of the exclusive concession granted to ICL by the State of Israel for the extraction of minerals from the Israeli side of the Dead Sea, in return for payment of royalties to the State. The costs of production of the potash and bromine extracted from the Dead Sea by ICL are relatively lower than the costs of other producers in the world who do not have access to the Dead Sea.

ICL's main production facilities are located in Israel, Germany, the United States, Holland, Spain, England, China, Brazil and France. Other production facilities are in Austria, Belgium, Turkey, Canada, Argentina, and Australia.

The overseas operations of ICL are mainly the manufacture of products which integrate with or are based on the operations of ICL in Israel or are closely related to them. Approximately 94% of ICL's products are sold outside Israel.

The activities of ICL's facilities are largely integrated with one another, both in terms of supply of raw materials and in the way in which one facility utilizes by-products of another facility to manufacture end products (for example, bromine is produced by utilizing the bromine present in the by-product streams from the evaporation ponds used to manufacture potash).

Approximately 6% of ICL's products are sold in Israel. For these sales, regarding certain products, ICL and some of the ICL companies have been declared a monopoly in Israel.

Approximately 50% of ICL's sales revenue stems from manufacturing operations outside Israel.

ICL has no material dependency on any single customer, supplier or source of raw materials that is not included in the concessions granted to ICL.

The three main segments of ICL's operations are grouped according to managerial-functional considerations, as follows:

- A. **ICL Fertilizers** – ICL Fertilizers produces potash from the Dead Sea and mines, and produces potash and salt from underground mines in Spain and England. ICL Fertilizers refines the potash into various grades and sells it worldwide, and uses some of it in the manufacture of complex fertilizers.
- ICL Fertilizers also mines and processes phosphate rock from open-pit mines in the Negev region, and manufactures sulfuric acid, fertilizer-grade phosphoric acid, phosphate fertilizers, complex fertilizers based mainly on potash and phosphate, and specialty fertilizers at its production facilities in Israel. ICL Fertilizers also manufactures fertilizers in Holland, Germany and Belgium. In addition ICL Fertilizers manufactures phosphate-based animal feed additives in Turkey and Israel. ICL Fertilizers markets its products worldwide. Its top sales destinations are Europe, Brazil, India, China and Israel.
- B. **ICL Industrial Products** – ICL Industrial Products manufactures bromine from an end-brine created as a byproduct of the potash production process in Sedom, as well as bromine-based compounds. ICL Industrial Products is the world's leading manufacturer of bromine, producing about 30% of total global production. ICL Industrial Products uses most of the bromine it produces for manufacturing bromine compounds at its production sites in Israel, Holland and China. In addition, ICL Industrial Products produces various salt, magnesia and chlorine products (chlorine is produced together with caustic soda by electrolysis of the salt created as a byproduct of potash production, and is used as a raw material in the segment's production processes). ICL Industrial Products also manufactures chlorine-based products in Israel and the USA. ICL Industrial Products markets its products worldwide.
- C. **ICL Performance Products** – ICL Performance Products purifies some of the fertilizer-grade phosphoric acid manufactured by ICL Fertilizers, purchases purified phosphoric acid from other sources, and also manufactures thermal phosphoric acid. The purified acid is used in the manufacture of downstream products of high added value – phosphate salts, food additives, hygiene products, phosphorus derivatives and flame retardants. ICL Performance Products also produces specialty products based on aluminum oxide (alumina) and other raw materials. Most of ICL Performance Products' production takes place at sites in Germany, the U.S.A., Brazil, Israel and China.

In addition to these segments, ICL activities include desalination and metallurgy.

Management by segment is accomplished on a managerial – functional basis, even where administrative structure and legal ownership do not fully correspond.

1.2 Business environment and profitability of ICL

ICL is a multinational company. Its business results are influenced by global economic trends, changes in trading and financing conditions, and fluctuations in exchange rates. The demand for ICL's products is influenced, inter alia, by the demand for basic agricultural products and by the global economic situation.

ICL takes steps to adjust its marketing and production policy to the circumstances in world markets.

ICL is focusing on improving its cash flow, diversifying its sources of financing and continuing with its savings and efficiency measures.

The vast majority of ICL's sales are made in foreign currency, mainly US dollars and the euro. A portion of its operating expenses in Israel are denominated in NIS. Therefore, devaluation of the NIS against the US dollar has a positive impact on ICL's profitability, while appreciation has the opposite effect. The strengthening of the Israeli shekel against the dollar adversely affected the operating income of ICL compared with the same period last year, by approximately \$20 million. ICL has more revenues than expenses in Euro. Therefore, appreciation of the Euro against the dollar has a positive impact on ICL's profitability, and devaluation has a negative impact. ICL hedges against some of its currency exposure. The appreciation of the euro against the US dollar adversely affects the competitiveness of ICL's subsidiaries whose operating currency is the euro, compared with companies whose operating currency is the dollar.

Most of ICL's debt bears variable interest. Therefore, ICL is exposed to fluctuations in interest rates. The Company partially protects against such exposure by using financial hedging instruments, including derivatives.

Conditions in the global agricultural market, which have a material effect on the demand for fertilizers, improved. Recent years have seen an upward trend in global consumption of grains (such as cereals, rice, soybean and maize), resulting from natural population growth and from the change in the

composition of food consumption (increased consumption of meat) as standards of living rise, especially in developing countries. In addition, the sharp rise in energy prices, environmental considerations and the aspiration of western countries to reduce dependence on imported fuel have resulted in an increasing global tendency to switch to fuel made from agricultural products (biofuels). These trends have led to a considerable rise in the prices of agricultural produce during the last year, an increase in the areas of grains planted worldwide and higher yields per agricultural unit, in particular by increased application of fertilizers. As a result, the demand for fertilizers increased and the prices of most types of fertilizers have risen sharply.

In June 2007 ICL Fertilizers signed agreements for the sale of potash to customers in India for a period of about one year. Under these agreements, ICL will supply up to approximately 1.1 million tons of potash (including optional quantities) in the amount of \$300 million, and at a price increase of \$50/ton compared to prices under the previous agreement. In Europe potash producers and customers signed contracts for supply of potash for the second half of 2007, at an increase of over €20/ton.

On August 2, 2007 a professional journal in the fertilizer industry published about an increase in potash prices resulting from an increase in demand¹. Potash producers in Brazil announced an additional price increase of \$25 per ton, commencing October 1, 2007. This increase is added to previous price increases, which sum up to a total price increase of \$125 compared with prices at the end of 2006 in Brazil. In Southeast Asia, potash producers announced a price increase of \$30 per ton in the last quarter of 2007, after prices already rose by \$40 per ton in the third quarter of 2007.

The bromine market is greatly influenced by the level of activity in the electronics and oil and gas - drilling markets, and by the restrictions imposed on the use of methyl bromide following implementation of the Montreal Protocol. The first half of 2006 was characterized by strong demand for flame retardants which paralleled the rise in demand for electronic products. Commencing in the third quarter of 2006, the demand for flame retardants slowed down, while concurrently, due to the relatively high prices of bromine and bromine compounds, Chinese production of bromine and some flame retardants increased. The trends in the first half of 2007 are similar to those which prevailed in the second half of 2006. Average selling prices of chemicals used for oil drilling rose in 2006 following the expiry at the end of 2005 of a long-term contract with low prices. Conversely, sales of these products dropped after agreements with two large customers were not renewed. This decline continued in the first half of 2007. The decline in sales of ICL Industrial Products has been influenced also by increased supply from Chinese producers, who added large quantities to the market.

The activity of ICL Performance Products is affected by competition in some of its target markets and by the rate of exchange. Appreciation in the average rate of exchange of the euro against the US dollar compared with the same quarter of last year, harmed competitiveness in some of its production activity in Europe. In the reporting period, revenue of ICL Performance Products increased as a result of higher sales and price increases for some of the products.

Marine transportation expenses are a significant component in the expenses of ICL Fertilizers. In 2006, the trend of sharp fluctuations in bulk marine transportation prices continued. In the first half of 2006, marine transportation prices dropped sharply, while in the second half of the year, prices rose, a trend which continued in the first half of 2007.

The increase in the selling prices of most types of fertilizers as noted above, was partially offset by the increase in transportation prices.

ICL Fertilizers exports its products through dedicated bulk facilities in Israel's ports (Ashdod and Eilat). The facilities were erected by ICL Fertilizers and are operated by the port companies. There have recently been disruptions in operating and loading at the ports, particularly Ashdod, which have caused delays in shipments at peak times. As a result, not all of the potash and fertilizers planned for sale was actually shipped. ICL Fertilizers is working with the port companies to regulate the operating framework in a way that solves these problems.

ICL Industrial Products exports most of its products in containers or isotanks (used for transporting acids), through Israel's ports. The products of Dead Sea Magnesium and specialty fertilizers of ICL Fertilizers are also shipped in containers, on container ships that regularly dock in Israel's ports and take responsibility for loading containers at the general piers of the ports. Due to disputes between port workers and management, there have been recent disruptions in the loading of containers, which have been damaging to various companies, including ICL.

¹ Reports in FMB, a professional journal of the fertilizer industry, August 2, 2007.

1.3 This Directors' Report is attached to the interim financial statements for the period ended June 30, 2007, on the assumption that those financial statements are before the reader. The Directors' Report is in a condensed format, since it is assumed that the reader also has access to the Periodic Report for 2006.

2. Results of Operations

2.1 Principal Financial Results

Hereunder the condensed results of operations in the reviewed period, compared with the results for the same period last year, in millions of dollars.

	1-6/2007		1-6/2006		4-6/2007		4-6/2006		2006	
	\$		\$		\$		\$		\$	
	\$	% of sales	\$	% of sales	\$	% of sales	\$	% of sales	\$	% of sales
Sales	1,845.8	100.0	1,564.2	100.0	962.9	100.0	847.3	100.0	3,258.2	100.0
Gross profit	653.8	35.4	538.8	34.4	349.0	36.2	273.1	32.2	1,153.2	35.4
Operating income	305.3	16.5	260.4	16.6	167.2	17.4	124.3	14.7	536.4	16.5
Pre-tax income	287.6	15.6	244.9	15.7	164.4	17.1	113.7	13.4	494.9	15.2
Net income	221.2	12.0	188.9	12.1	125.8	13.1	92.3	10.9	373.9	11.5
Cash flow from current operations	269.1	14.6	140.3	9.0	182.4	18.9	94.1	11.1	358.6	11.0
EBITDA*	406.5	22.0	356.6	22.8	221.6	23.0	174.1	20.5	735.7	22.6
Investments in property, plant and equipment, less grants	85.9		62.9		26.3		31.8		141.0	

(*) Calculated as follows in millions of dollars:

	<u>1-6/2007</u>	<u>1-6/2006</u>	<u>4-6/2007</u>	<u>4-6/2006</u>	<u>2006</u>
Net earnings	221.2	188.9	125.8	92.3	373.9
Depreciation and deductions	94.3	86.4	48.7	43.7	174.5
Financing expenses, net	14.9	18.5	4.4	12.5	39.3
Taxes on income	72.9	62.8	42.7	25.6	136.7
Special or one-off expenses	3.2	-	-	-	11.3
Total	<u>406.5</u>	<u>356.6</u>	<u>221.6</u>	<u>174.1</u>	<u>735.7</u>

2.2 Results of operations: January – June 2007

Sales

Sales in the reporting period amounted to \$1,845.8 million, compared with \$1,564.2 million in the same period last year, an increase of approximately 18%. The increase reflects mainly an increase in the selling price as well as increased sales of potash and phosphate fertilizers, which were offset by a decline in the sales of some of the bromine compounds.

Below is a breakdown of sales by geographical region:

Sales CIF	1-6/2007		1-6/2006		2006	
			\$ millions	%	\$ millions	%
Israel	115.6	6.3	102.0	6.5	207.4	6.4
North America	366.9	19.9	374.7	24.0	717.8	22.0
South America	210.8	11.4	128.0	8.2	331.0	10.2
Europe	725.7	39.3	618.7	39.5	1,203.5	36.9
Asia	366.2	19.8	276.9	17.7	678.8	20.8
Rest of the world	60.6	3.3	63.9	4.1	119.7	3.7
Total	1,845.8	100.0	1,564.2	100.0	3,258.2	100.0

The breakdown of sales in the first half of 2007 shows an increase in sales in particular in South America, Europe and Asia. This increase stems mainly from the increased sales in the fertilizer segment to these regions.

Gross profit

Gross profit amounted to \$653.8 million, an increase of \$115.0 million compared with the same period last year. The gross profit out of sales turnover was 35.4% compared with 34.4% in the same period last year.

The increase in gross profit compared with the same period last year stems mainly from the rise in the selling price of potash and phosphate fertilizers and higher sales of these products. Conversely, the increase in gross profit was offset by the decline in production and sales of some bromide compounds, by an increase in shekel expenses in dollar terms, as a result of the appreciation of the shekel against the dollar and by an increase of some components of cost of production.

Sales and marketing expenses

Sales and marketing expenses amounted to \$259.2 million, an increase of about \$57.6 million compared with the same period last year. The increase in these expenses stems from an increase in sales of potash and fertilizers in which the transportation component is high, and a decline in sales of bromine compounds in which the transportation component is relatively low, and from a rise in the prices of bulk marine transportation. In addition, shekel expenses increased in dollar terms, as a result of the strengthening of the shekel against the dollar.

General and administrative expenses

General and administrative expenses totalled \$71.1 million, an increase of about \$11.1 million compared with the same period last year. The strengthening of the shekel and the euro against the dollar led to an increase in expenses in this item in dollar terms. In addition, administrative expenses include an expense of approximately \$3.6 million due to spreading of the benefit inherent in the stock options plan published at the beginning of 2007 over the term of entitlement, as required under Standard 24.

Research and development expenses

R&D expenses (net of grants from the Chief Scientist) amounted to \$18.3 million, an increase of \$1.4 million compared with the same period last year. The increase stems from increased R&D expenses in the Performance Products segment, and from an increase in shekel expenses in dollar terms as a result of appreciation of the shekel against the dollar.

Operating income

Operating income increased by 17.2% compared with the same period last year, reaching \$305.3 million. The increase stems from the increase in gross profit noted above, which was partially offset by an increase in overhead which was due, among other things, to the appreciation of the shekel against the dollar, and from an increase in transportation expenses.

Financing expenses

Net financing expenses amounted to approximately \$14.9 million, compared with \$18.5 million last year, a decrease of \$3.6 million. Income of exchange rate differences amounting to \$6 million, which stemmed from fluctuation in the NIS/USD exchange rate in the second quarter, was included in the reporting period. This gain was partially offset by an increase in the dollar interest rate.

Other net expenses

Other net expenses amounted to \$2.8 million. These expenses reflect mainly an update of pension provisions.

Tax expenses

Tax expenses amounted to \$72.9 million, compared with \$62.8 million last year. The tax rate on pre-tax profit was 25.3%, compared with 25.6% in the same period last year.

Net earnings

Net earnings amounted to \$221.2 million, compared with \$188.9 million in the same period last year, and increase of 17.1%.

2.3 Results of operations: April – June 2007

Sales

Sales of ICL in the quarter amounted to \$962.9 million, compared with \$847.3 million last year, an increase of approximately 13.6%.

The increase in the Group's sales is mainly due to the increased revenues in the fertilizer segment as a result of higher quantities of potash and fertilizers sold as well as an increase in prices. Sales of ICL Performance Products also increased. Conversely, the decline in sales of bromine compounds offset part of the increased sales.

Below is a breakdown of sales by geographical region:

	4-6/2007		4-6/2006	
	\$ millions	%	\$ millions	%
Israel	63.6	6.6	55.1	6.5
North America	187.5	19.5	198.5	23.4
South America	143.1	14.9	90.8	10.7
Europe	349.4	36.3	316.2	37.3
Asia	196.3	20.4	152.3	18.0
Rest of the world	23.0	2.3	34.4	4.1
Total	962.9	100.0	847.3	100.0

The increased sales of potash and fertilizers, both quantities and as a result of the increased prices, led to an increase in sales in South America, Europe and Asia.

The decrease of sales in North America stems from the decline sales of ICL Industrial Products, mainly clear brines for oil drilling and flame retardants.

Gross profit

Gross profit amounted to \$349.0 million, an increase of \$27.8% compared with the same quarter last year. The gross profit margin out of sales turnover increased from 32.2% to 36.2%.

The increase in profit and improved profit margin stems mainly from the increased sales and higher selling prices of potash and fertilizers.

Sales and marketing expenses

Sales and marketing expenses amounted to \$136.2 million, an increase of about 26.0% compared with the same period last year, mainly as a result of the increase in sales of fertilizers.

General and administrative expenses

General and administrative expenses totalled \$36.8 million, an increase of about \$4.6 million compared with the same period last year. This is mainly due to the appreciation of the shekel against the dollar and an expense of approximately \$2.7 million due to spreading of the benefit inherent in the stock options plan published at the beginning of 2007 over the term of entitlement, as required under Standard 24.

Research and development expenses

R&D expenses (net of grants from the Chief Scientist) amounted to \$8.8 million, similar to expenses in the same period last year.

Operating income

Operating income in the quarter increased by \$42.9 million compared with the same period last year, reaching \$167.2 million, an increase of 34.5%. The operating income rate from the sales turnover amounted to 17.4% compared to 14.7% last year.

Financing expenses

Net financing expenses amounted to \$4.4 million, compared with \$12.5 million in the same quarter last year.

The decrease is mainly due to income of \$7.5 million recorded in the second quarter of 2007 from exchange rate differences stemming from the appreciation of the shekel against the dollar.

Taxes on income

Taxes expenses in the report period amounted to \$42.7 million, which is 26.0% of the pre-tax profit.

Net earnings

Net earnings amounted to \$125.8 million, compared with \$92.3 million in the same period last year, an increase of 36.3%.

3. Segments of Operation

The segments of operation of ICL are presented below according to the managerial division into segments described in the preface to this report.

Sales CIF by operating segment	1-6/2007		1-6/2006		4-6/2007		4-6/2006	
	\$ millions	% of total sales	\$ millions	% of total sales	\$ millions	% of total sales	\$ millions	% of total sales
ICL Fertilizers	933.2	47.7	652.5	38.9	481.4	47.2	364.6	40.4
ICL Industrial Products	413.0	21.1	468.3	27.9	216.0	21.2	248.5	27.5
ICL Performance Products	527.4	27.0	497.5	29.7	278.4	27.3	255.3	28.3
Others and setoffs	(27.8)		(54.1)		(12.9)		(21.1)	
Total	1,845.8		1,564.2		962.9		847.3	

Note: The sales data for the segments and their percentages out of total sales are before setoffs of inter-segment sales.

Operating income by operating segment	1-6/2007		1-6/2006		4-6/2007		4-6/2006	
	\$ millions	% of total sales	\$ millions	% of total sales	\$ millions	% of total sales	\$ millions	% of total sales
ICL Fertilizers	186.4	20.0	102.0	15.6	110.6	23.0	47.4	13.0
ICL Industrial Products	81.9	19.8	131.2	28.0	36.5	16.9	69.1	27.8
ICL Performance Products	44.8	8.5	41.9	8.4	26.0	9.3	17.2	6.7
Others and setoffs	(7.8)		(14.7)		(5.9)		(9.4)	
Total	305.3	16.5	260.4	16.6	167.2	17.4	124.3	14.7

Note: The earnings percentage is out of total sales, before setoffs of inter-segment sales.

3.1 ICL Fertilizers

Sales

The volume of sales in the segment in 2007 amounted to approximately \$933.2 million, an increase of about 43.0%. The increase in sales turnover stems from an increase in potash prices and a sharp increase in sales of potash compared with the same period last year, when sales of potash decreased due to protracted negotiations with Chinese and Indian customers. In addition, larger quantities of phosphate fertilizers were sold, and their prices rose compared with the same period last year.

Operating income

Operating income in the segment amounted to approximately \$186.4 million, an increase of about 82.7% compared with the same quarter in 2006. The percentage of operating income out of sales was approximately 20.0%, compared with 15.6% last year.

The increase in operating income stems from the increase in revenue as aforesaid. Conversely, operating income was adversely affected by an increase in expenses and in particular by the appreciation of the shekel against the dollar and by a sharp rise in marine transportation prices.

Potash

Revenues from the segment includes sales by Dead Sea Works (excluding the operations of Dead Sea Salts), Iberpotash and Cleveland Potash.

Potash – Revenue and Income

\$ millions	1-6/2007	1-6/2006	4-6/2007	4-6/2006	2006
Revenue*	579.4	391.4	303.5	214.3	925.1
Operating income	145.6	93.6	79.4	42.2	245.1

* Including revenue from inter-segment sales.

The increase in revenue compared with the same period last year stems from a significant increase in the quantity of potash sold and an increase in the sales price compared to the same period last year.

Potash – Production and Sales

Thousands of tons	1-6/2007	1-6/2006	4-6/2007	4-6/2006	2006
Production	2,393	2,500	1,167	1,242	5,086
Sales to external customers	2,413	1,577	1,239	901	3,912
Sales to internal customers	122	115	72	65	236
Total sales (including internal sales)	2,535	1,692	1,311	966	4,148

The decrease in potash production stems mainly from the decrease in production in Israel and in England mainly due to periodical maintenance work performed at these plants. At the beginning of 2006 the Suria mine in Spain has been closed. ICL Fertilizers is considering a number of options for further reorganization of its mining operations in Europe.

Fertilizers and Phosphates

Sales revenue for these items stems from sales in Israel and abroad of phosphate rock (as a raw material and for direct fertilization), fertilizers (including phosphate, compound, liquid and fully soluble fertilizers, which include differing proportions of nitrogen, phosphorus and potassium), phosphoric acid used as a raw material for the production of fertilizers (green acid), as well as other products.

Fertilizers and Phosphates – Sales Revenue and Income

Millions of dollars	1-6/2007	1-6/2006	4-6/2007	4-6/2006	2006
Revenue*	375.5	280.7	191.2	161.7	594.4
Operating income	41.1	7.9	31.7	6.1	19.8

* including inter-segment sales

Revenue in the quarter is higher than in the previous year due to an increase in quantities sold and in the selling prices of fertilizers.

The improvement in operating income stems from a rise in selling prices and increased quantities of fertilizers sold. Conversely, operating income was adversely affected by appreciation of the shekel against the dollar and a rise in marine transportation prices of bulk.

Fertilizers and Phosphates – Production and Sales

Thousands of tons	1-6/2007	1-6/2006	4-6/2007	4-6/2006	2006
<u>Phosphate rock</u>					
Production	1,493	1,520	765	762	2,949
Sales*	177	257	79	204	421
<u>Fertilizers</u>					
Production	861	770	463	387	1,614
Sales*	951	762	446	406	1,656

* external customers (excluding sales to Group – companies)

Phosphate rock is produced according to demand, both for internal uses and for sales to outside customers, while maintaining suitable stock levels. The volume of sales of rock in the period stems partially from the segment's policy of diverting most of the output to internal uses of higher added value in the manufacture of acids and fertilizers.

In the period there was a sharp increase in sales of phosphate fertilizers compared with the same period last year, as a result of the increased demand in Brazil and Europe.

3.2 ICL Industrial Products

Sales

Sales in this segment in the reporting period amounted to approximately \$413.0 million, a decrease of about \$55.3 million compared with the same period last year. The decrease in sales, compared to the same period last year, stems from smaller quantities sold, which was partially offset by the higher selling prices of some of the products.

Sales in the second quarter amounted to \$216.0 million, a decrease of 13.1% compared to the same quarter last year. The decrease in sales was mainly in sales of flame retardants to the electronics market and sales of clear brines to the oil and gas drilling market.

Revenue from flame retardants decreased during the period due to smaller quantities sold following a slowdown in the printed circuits market and intensifying competition from Chinese producers.

Revenue from inorganic bromine products decreased for the period, particularly clear brines, as a result of a decrease in quantity sold.

Sales of agricultural products decreased in quantities sold in the period compared with last year, due to implementation of the Montreal Protocol.

In biocides for water treatment, revenue decreased, mainly due to the relatively cool summer in North America.

Revenue from sales of chlorine-based products from the Dead Sea (Dead Sea Salts) increased slightly, mainly due to larger sales of magnesium chloride.

An increase was recorded in sales of magnesia products, particularly calcined and special products.

Operating income

Operating income in the segment for the reporting period was approximately \$81.9 million, a decrease of about 37.6% compared with the same period last year.

The decrease stems mainly from a decrease in quantities sold and also in the quantity produced, which was planned to adjust production to demand. Operating income was also adversely affected by a rise in shekel expenses, particularly as a result of the appreciation of the shekel against the dollar and by the rise of some components of production cost.

3.3 ICL Performance Products

Sales

Sales in this segment amounted to approximately \$527.4 million, an increase of about 6% compared with the same period last year.

The increase in revenue stems mainly from the appreciation of the euro against the dollar, a slight increase in the quantities sold of some of the products in Europe and the increase in the selling price of some of the products.

Operating income

Operating income in the segment in the reporting period amounted to approximately \$44.8 million, an increase of about 6.9% compared with the same period last year. The profit from sales was approximately 8.5%, compared with 8.4% in the same quarter last year. The increase in operating income stems from the increase in sales and operational streamlining which was compensated by increased cost of raw materials.

4. Financial position and sources of financing of ICL

In the reporting period, ICL recorded an increase of \$159 million in net financial liabilities compared with their balance at the end of 2006. At the end of June 2007 net financial liabilities amounted to \$711 million.

ICL's sources of financing are primarily short- and long- term loans from Israeli and international banks.

After the balance sheet date, on August 6, 2007, ICL entered into an agreement with a group of 17 banks in Europe, the USA and Israel. Under the agreement, the banks will grant ICL a loan of \$725 million for a period of five years (bullet repayment on maturity) bearing interest of short-term Libor + 0.45%. The new loan will replace, inter alia, a similar borrowing facility of 2005 for \$250 million at an interest rate of Libor + 0.6% for five years and which will now be repaid ahead of its original maturity.

After the balance sheet, in July 2007, ICL increased its trade-receivables securitization facility (signed in 2004 with Rabobank), in which some of the Group's companies sell their trade receivables to a foreign company which was set up for this purpose, and which is neither owned nor controlled by the ICL Group (SPV). The additional amount is \$80 million and the new total amount of the facility is \$300 million.

Cash flow

The cash flow of ICL from current operations in the period amounted to \$269.1 million, compared with \$140.3 million in the same period last year, an increase of \$128.8 million. The cash flow for the period includes insurance payments received, which were recorded as income last year and were actually received in this period. Conversely, the increase in sales also led to an increase in trade receivables, which had a negative effect on available cash from current operations. Cash flow from current operations together with the increase in net financial liabilities of \$159 million were the principal source of finance for investments in fixed assets of \$86 million, and for paying dividend payments to the shareholders of about \$350 million.

Insurance

At the beginning of the second quarter, ICL increased its insurance coverage for physical damage and for consequential loss to its property due to earthquake, from \$575 million to \$600 million, on standard terms in the industry.

5. Investments

In the reporting period, investments in property, plant and equipment net of investment grants amounted to approximately \$85.9 million, compared with investments in property, plant and equipment less grants amounting to \$62.9 million in the same period last year.

6. Human Resources

The total number of employees at ICL as on June 30, 2007 is 9,620, compared with 9,312 on June 30, 2006. The increase in the number of employees stems mainly from reclassifying workers in the ICL Industrial Products segment from contract workers to employees, the growth in the ICL Performance Products segment following acquisition of Fire-Trol assets in Canada and reinforcement of staff in North-America due to the fire season in the USA and Canada. There was also an increase in the number of employees at Israel Desalination Engineering (IDE).

7. Market Risk Exposure and Management

Below is an update of the sensitivity to changes in the exchange rates for the first half of 2007:

Sensitivity to changes in exchange rates

Millions \$ (NIS/USD) Instrument type	Profit (loss) from changes		Fair value	Profit (loss) from changes	
	Rise of 10%	Rise of 5%		Fall of 5%	Fall of 10%
Cash and cash equivalents	(0.1)	(0.1)	1.6	0.1	0.2
Marketable securities	0.0	0.0	0.0	0.0	0.0
Short-term deposits and loans	(0.3)	(0.2)	3.6	0.2	0.4
Other receivables	(7.2)	(3.7)	78.7	4.1	8.7
Inventories	0.0	0.0	0.0	0.0	0.0
Financial investments in associated companies	0.0	0.0	0.0	0.0	0.0
Long-term deposits and loans	(0.4)	(0.2)	4.9	0.3	0.5
Credit from banks and others	9.5	5.0	(104.6)	(5.5)	(11.6)
Suppliers and others	10.6	5.6	(116.8)	(6.1)	(13.0)
Other payables	17.5	9.1	(192.1)	(10.1)	(21.3)
Employee related obligation	10.2	5.3	(112.0)	(5.9)	(12.4)
Long-term bank loans	0.0	0.0	0.3	0.0	0.0
Debentures	0.0	0.0	0.0	0.0	0.0
			-		
Options	(12.8)	(10.2)	(4.1)	10.4	21.2
Forward	(0.9)	(0.5)	0.0	0.5	1.1
Total	27	11	(441)	(13)	(27)

Millions \$ (EUR/USD)	Profit (loss) from changes		Fair value	Profit (loss) from changes	
	Rise of 10%	Rise of 5%		Fall of 5%	Fall of 10%
Instrument type					
Cash and cash equivalents	(0.8)	(0.4)	9.1	0.5	1.0
Marketable securities	0.0	0.0	0.0	0.0	0.0
Short-term deposits and loans	(7.6)	(4.0)	83.3	4.4	9.3
Other receivables	(19.3)	(10.1)	212.2	11.2	23.6
Inventories	(13.4)	(7.0)	147.7	7.8	16.4
Financial investments in associated companies	(8.9)	(4.7)	98.2	5.2	10.9
Long-term deposits and loans	(0.4)	(0.2)	4.3	0.2	0.5
Credit from banks and others	11.2	5.9	(123.3)	(6.5)	(13.7)
Suppliers and others	11.6	6.1	(127.7)	(6.7)	(14.2)
Other payables	9.9	5.2	(108.8)	(5.7)	(12.1)
Employee related obligation	9.3	4.9	(102.6)	(5.4)	(11.4)
Long-term bank loans	2.1	1.1	(22.9)	(1.2)	(2.5)
Forward	(6.5)	(4.6)	(2.6)	2.3	4.8
Options	(1.6)	(2.1)	(0.7)	2.0	5.7
Total	(14.4)	(10.1)	66.3	8.0	18.2

Millions \$ (GBP/USD)	Profit (loss) from changes		Fair value	Profit (loss) from changes	
	Rise of 10%	Rise of 5%		Fall of 5%	Fall of 10%
Instrument type					
Cash and cash equivalents	(0.2)	(0.1)	1.7	0.1	0.2
Marketable securities	0.0	0.0	0.0	0.0	0.0
Short-term deposits and loans	(0.5)	(0.2)	5.2	0.3	0.6
Other receivables	0.9	0.5	(9.7)	(0.5)	(1.1)
Inventories	(1.7)	(0.9)	18.7	1.0	2.1
Financial investments in associated companies	0.0	0.0	0.0	0.0	0.0
	0.0	0.0	0.0	0.0	0.0
Credit from banks and others	1.0	0.5	(10.9)	(0.6)	(1.2)
Suppliers and others	0.9	0.5	(10.0)	(0.5)	(1.1)
Other payables	2.2	1.2	(24.5)	(1.3)	(2.7)
Employee related obligation	(0.3)	(0.2)	3.5	0.2	0.4
Total	2.4	1.2	(26.0)	(1.4)	(2.9)

Sensitivity to changes in Libor

Millions \$	Profit (loss) from changes		Fair value	Profit (loss) from changes	
	5.907	5.6385		5.1015	4.833
Interest Libor variable Instrument type	<u>Rise of 10%</u>	<u>Rise of 5%</u>		<u>Fall of 5%</u>	<u>Fall of 10%</u>
Loans at fixed interest	4.2	2.1	(211.4)	(2.1)	(4.2)
Loans at variable interest			(719.6)		
Collar transactions	0.6	0.3	1.807	(0.2)	(0.4)
Cap options	0.2	0.0	1.471	(0.3)	(0.5)
Swap transactions	(2.6)	(1.3)	(4.8)	1.3	2.6
Total	2.4	1.1	(932.5)	(1.4)	(2.6)

Millions \$ (JPY/USD)	Profit (loss) from changes		Fair value	Profit (loss) from changes	
	<u>Rise of 10%</u>	<u>Rise of 5%</u>		<u>Fall of 5%</u>	<u>Fall of 10%</u>
Cash and cash equivalents	(0.1)	0.0	0.7	0.0	0.1
Marketable securities	0.0	0.0	0.0	0.0	0.0
Short-term deposits and loans	0.0	0.0	0.0	0.0	0.0
Other receivables	(1.4)	(0.7)	15.4	0.8	1.7
Inventories	(1.0)	(0.5)	10.6	0.6	1.2
Financial investments in associated companies	0.0	0.0	0.0	0.0	0.0
Long-term deposits and loans	0.0	0.0	0.1	0.0	0.0
Credit from banks and others	0.2	0.1	(2.1)	(0.1)	(0.2)
Suppliers and others	0.3	0.1	(3.1)	(0.2)	(0.3)
Other payables	0.0	0.0	0.2	0.0	0.0
Employee related obligation	0.1	0.1	(1.2)	(0.1)	(0.1)
Forward	1.7	1.1	0.5	(0.7)	(1.4)
Options	1.0	0.5	0.4	(0.5)	(0.9)
Total	0.8	0.7	21.2	(0.1)	0.0

Millions \$) (Real Brazil/USD Instrument type	Profit (loss) from changes		Fair value	Profit (loss) from changes	
	Rise of 10%	Rise of 5%		Fall of 5%	Fall of 10%
Cash and cash equivalents	(0.3)	(0.1)	3.1	0.2	0.3
Marketable securities	0.0	0.0	0.0	0.0	0.0
Short-term deposits and loans	0.0	0.0	0.0	0.0	0.0
Other receivables	(0.5)	(0.2)	5.1	0.3	0.6
Inventories	(0.6)	(0.3)	7.0	0.4	0.8
Financial investments in subsidiaries	(0.9)	(0.5)	9.5	0.5	1.1
	0.0	0.0	0.0	0.0	0.0
Credit from banks and others	0.0	0.0	0.0	0.0	0.0
Suppliers and others	0.2	0.1	(2.4)	(0.1)	(0.3)
Other payables	0.2	0.1	(2.0)	(0.1)	(0.2)
Total	(1.9)	(1.0)	20.4	1.1	2.3

Update of the derivative position for the first half of 2007:

Hedging transactions against changes in the exchange rates on cash flows

In thousands of dollars	Nominal value up to one year		Fair value up to one year	
	Long	Short	Long	Short
Direction of transaction in derivatives is dollar purchase				
Currency: Euro/USD				
Forward				
Recognized for accounting purposes	29,039		(1,071)	
Recognized for accounting purposes for more than one year	16,000		(1,508)	
Call options				
Recognized for accounting purposes	78,508		1,010	
Put options				
Recognized for accounting purposes	76,059		267	
Currency: JPY/USD				
Forward				
Recognized for accounting purposes	12,975		521	
Call options				
Recognized for accounting purposes	14,500		479	
Put options				
Recognized for accounting purposes	14,500		(93)	

In thousands of dollars	Nominal value up to one year		Fair value up to one year	
	Long	Short	Long	Short
Currency: NIS/USD				
Call options				
Recognized for accounting purposes		319,100		(5,749)
Put options				
Recognized for accounting purposes		212,600		1,610
Forward				
Recognized for accounting purposes		10,000		11

**Interest-hedging transactions - for hedging changes in variable interest rate
(Libor) on dollar loans**

\$000	Nominal value				Fair value			
	Up to one year		Over one year		Up to one year		Over one year	
	Long	Short	Long	Short	Long	Short	Long	Short
Swap				125,000				(4,771)
Caps	56,000		450,000		352		2,925	
Floors	6,000		350,000					

8. Accounting issues

8.1 Adoption of International Financial Reporting Standards (IFRS)

In July 2006 the Israel Accounting Standards Board published Accounting Standard No. 29 – Adoption of International Financial Reporting Standards (IFRS) (hereinafter – Standard 29). Standard 29 stipulates that companies that are subject to the provisions of the Israeli Securities Law 5728-1968 and that are required to report according to the standards of that law, will prepare their financial statements under IFRS as of January 1, 2008 (financial statements for the first quarter of 2008). Standard 29 allows early adoption of IFRS, commencing from the financial statements to be published after July 31, 2006.

First-time adoption of IFRS will be in accordance with the provisions of IFRS 1 in respect of first time adoption of IFRS. Financial statements prepared under IFRS in the first year of adoption require presentation of comparative figures for one year only.

In addition, Standard 29 requires companies drawing up their financial statements under IFRS for the first time after January 1, 2008 to disclose, in a note to their financial statements for 2007 (prepared in accordance with generally accepted accounting principles in Israel), the balance sheet data as of December 31, 2007 and statement of income data for the year ended December 31, 2007, as they would appear after applying IFRS recognition, measurement and presentation rules.

The Company and its subsidiaries are preparing to adopt IFRS, and in this framework the Company is assessing the material impact expected on the Group's companies following the transition.

Stages of adoption determined by the Company's management:

Actions taken up to publication of the 2Q financial statements for 2007:

- Review of IFRS
- Mapping of IFRS relevant to the Company and in-depth examination of their expected impact on the financial statements.
- Defining uniform accounting policy for the Company and its subsidiaries, to be applied in the Company's consolidated reports.
- Selection of the relief provided by IFRS 1, to be applied in all the Group's companies.
- Actuary assessments for liabilities for employee severance and other post-employment benefits, net for the transition.
- Identification of material contracts, engagements or agreements that could be affected as a result of adoption of IFRS.

Action to be taken prior to the publication of the annual financial statements as of December 31, 2007:

- Completion of the qualitative and quantitative assessment of any further implications, due to the adoption of IFRS
- Submission of the material to the auditors for auditing the opening numbers for January 1, 2007
- Preparation of the balance sheet for December 31, 2007 under IFRS and preparation of the statement of income for 2007 under IFRS
- Preparation of interim financial statements for the first three quarters of 2007 under IFRS

Below is a description of the estimated material financial implications of the transition to IFRS on the Group's financial position as of January 1, 2007 (transition date) and on the results of the operations for a period of six months ending June 30, 2007. The description is presented in a format of adjustment between the amounts in the consolidated financial statements as reported under Israeli GAAP and the amount as if reported under IFRS.

As the impact of the transition to IFRS on the balance sheet for June 30, 2007 is not materially different from December 31, 2006, the financial impact of the transition to IFRS on the results of the Group for June 30, 2007 have not been included.

It is emphasized that the information presented below is based on assessments and estimations as of the report date and there could be changes after further information is collected and adjusted to IFRS principles, and changes stemming from developments in relation to IFRS interpretations. As the first financial statements prepared under IFRS in the financial statements will be approved in the future, it is possible that the board of directors will change the accounting policy on which this information is based. It is also emphasized that the information below is neither reviewed nor audited.

8.1.1 Items in the balance sheet which will be materially affected by transition to IFRS

	Note	January 1, 2007		
		Israeli GAAP*	Effect of transition to IFRS	IFRS
\$ thousands				
Current assets				
Cash and cash equivalents		50,085	-	50,085
Short-term investments, deposits and loans	3,9	120,820	(250)	120,570
Trade receivables	2	470,569	218,482	689,051
Other receivables	3,6	180,869	(35,596)	145,273
Inventories		785,433	-	785,433
		<u>1,607,776</u>	<u>182,636</u>	<u>1,790,412</u>
Long term Investments , loans and receivables				
Associated companies	9	31,149	1,735	32,884
Long term deposits and receivables	1,3,9	27,798	(966)	26,832
Inventories – non-current		33,865	-	33,865
Receivables from minority interest	4	17,011	(17,011)	-
Property, plant and equipment, net	5	1,688,954	(4,614)	1,684,340
Other assets and deferred expenses, less accumulated amortization	5	195,450	4,833	200,283
Deferred income taxes, net	1,6	6,539	46,437	52,976
		<u>2,000,766</u>	<u>30,414</u>	<u>2,031,180</u>
		<u>3,608,542</u>	<u>213,050</u>	<u>3,821,592</u>
Current liabilities				
Credit from banks and others	2	266,973	218,482	485,455
Trade payables		315,945	-	315,945
Other payables	1,3,6	371,348	2,240	373,588
		<u>954,266</u>	<u>220,722</u>	<u>1,174,988</u>
Long-term liabilities				
Loans from banks and others		358,391	-	358,391
Debentures		125,000	-	125,000
Provision for reclamation of mines and disposal of waste		24,989	-	24,989
Deferred income taxes, net	6,9	168,391	3,222	171,613
Liability for employee severance and other post-employment benefits, net	1	241,252	48,883	285,135
		<u>918,023</u>	<u>47,105</u>	<u>965,128</u>
Minority interests	4	9,476	(9,476)	-
Shareholders' Equity				
Shareholders' Equity		1,726,777	(37,766)	1,689,011
Minority interests	4	-	(7,535)	(7,535)
		<u>1,726,777</u>	<u>(45,301)</u>	<u>1,681,476</u>
		<u>3,608,542</u>	<u>213,050</u>	<u>3,821,592</u>

* Restated due to first time adoption of new Israeli standards

8.1.2 Items in the statements of income which will be materially affected by transition to IFRS

\$ thousands	For the six month period ended June 30, 2007			
	Note	Israeli GAAP	Effect of transition to IFRS	IFRS
Sales	3,8	1,845,827	210	1,846,037
Cost of sales	1,3,8	1,191,993	1,298	1,193,291
Gross profit		653,834	(1,088)	652,746
R&D expenses, net	1,3,8	18,329	125	18,454
Sales and marketing expenses	1,3,8	259,154	537	259,691
General & administrative expenses	1,3,8	71,066	(1,098)	69,968
		348,549	(436)	348,113
Operating income		305,285	(652)	304,633
Other income (expenses), net	8	2,774	(2,786)	(12)
Financial expenses, net	1,3	14,879	6,993	21,872
Income before taxes on income		287,632	(4,859)	282,773
Taxes on income	1	72,943	(1,548)	71,395
Income after taxes on income		214,689	(3,311)	211,378
Share in profits of associated companies, net		1,973	-	1,973
Minority interest in losses (income) of subsidiaries, net	4	4,570	4,570	-
Net profit		221,232	(7,881)	213,351

8.1.3 The items in the statement on changes in equity for the six month period ended June 30, 2007 that are expected to be materially affected by the transition to IFRS

\$ thousands	For the six month period ended June 30, 2007			
	Note	Israeli GAAP	Effect of transition to IFRS	IFRS
Earnings – net earnings for the period		221,232	(7,881)	213,351
Minority interests	4	-	4,570	4,570

8.1.4 Notes of the quantitative impact of transition according to IFRS 1

1) Liabilities for employee severance and other post-employment benefits, net

Under Israeli GAAP, liabilities for severance pay are based on a multiple of the number of years of employment and the last monthly salary of the employee (one month's salary for each year employed). The contributions to the funds are measured in accordance with their redemption value as at each balance sheet date.

Under IFRS, severance liability is calculated in accordance with International Accounting Standard 19 (IAS 19) in respect of employee benefits. Under the provisions of IAS 19, part of the Group's severance pay plan constitutes a defined benefit plan as defined under IAS 19. Liability for employer-employee relations in this plan are estimated in accordance with actuarial

assessment and take into account, inter alia, future increase in salaries and employee turnover. Measurement is made on the basis of capitalized amounts of the expected future cash flows, in accordance with the interest rate of company debentures with high rating. In addition, the contributed deposits are measured in accordance with their current fair value, taking into account expected future yields on the assets of the plan.

One of the Company's foreign subsidiaries has a liability for pension to employees that were calculated in accordance with Israeli GAAP on the basis of actuarial assessments whereas part of the actuarial gains and losses were not recognized in the financial statements on the basis of the "corridor" approach. The company selected as its accounting policy one of the alternatives allowed under IAS 19, to account for actuarial gains and losses. On the basis of the alternative selected actuarial gains and losses will be recognized immediately in shareholder's equity (retained earnings).

In addition, expenses included as salaries and related expenses under Israeli GAAP are charged as financing expenses under IFRS. These expenses include, amongst others, interest income and revaluation of the assets of the plan.

The net effect of the transition to IFRS on measuring liability for employee severance and other post-employment benefits, net, as at the transition date, is reflected in an increase of \$43,883 thousand. In addition, adjustment of the liability as at the transition date resulted in a decrease in deferred taxes in the amount of \$2,615 thousand.

The effect of the change in measuring liability for employee severance and other post-employment benefits, net, on the statement of income for the six month period ended June 30, 2007 is reflected in a decrease in salary expenses of \$1,117 thousand, an increase in financing expenses of \$3,245 thousand and a decrease in tax expenses of \$527 thousand.

2) Securitization transactions

The Company and some of the Group's subsidiaries engaged in a securitization agreement, under which the companies sell certain of their trade receivables to a foreign company which was set up especially for this purpose and which is neither owned nor controlled by the Group (hereinafter: the Acquiring Company). The Acquiring Company finances acquisition of the debts by means of a loan from a financial institution, which is not related to the Company, which finances the loan out of the proceeds of commercial papers that it issues on the US commercial paper market.

According to Israeli GAAP, which is based on US standard FAS 140, the Group's securitization transaction complied with the true sales definition and therefore receivables included in the securitization transaction were derecognized in the consolidated financial statements..

The Company's securitization transaction does not comply with the conditions for derecognition of financial assets defined under IAS 39 for financial instruments – measurement, as the Group did not transfer all the risks and benefits derived from the receivables. Therefore in the transition to IFRS, receivables included in the securitization transaction were recorded in the consolidated balance sheet as receivables. Conversely, in accordance with IFRS, consideration received from the foreign company under the securitization agreement will be recorded as a financial liability.

Accordingly, in the transition to IFRS, there was an increase in the customer balance as of the transition date in the amount of \$218,482 thousand. Conversely, the financial liability was increased by the same amount.

3) Hedging transactions

The Company uses financial instruments, including derivative financial instruments, to reduce exposure to exchange rate and interest rate risks.

According to established practice in Israel, the terms for applying hedging accounting are based mainly on economic criteria. In addition, due to certain circumstances financial derivatives used for hedging are not reflected in the balance sheet.

International Accounting Standard IAS 39 states that in order for a financial instrument to comply for hedging treatment it must comply with a number of conditions, designation of the instrument, strict documentation and expectation for high hedging effectiveness.

The changes in the fair value of the financial instrument designated for hedging of the asset or liability will be charged in the statement of income together with a corresponding charge for the

changes in the fair value of the defined asset or liability relating to the hedged risk. In addition, under the international standard, changes in the fair value for derivative financial instruments that do not meet the terms required for hedging accounting will be immediately charged to the statement of income.

The Company's transactions in financial instruments to reduce exposure, as aforesaid, do not comply with the hedging terms defined in the international standard and therefore in the transition to IFRS, these financial instruments are measured in accordance with their fair value while the changes in the fair value are immediately charged to the statement of income.

The impact of adoption of the provisions of the international standard in respect of hedging transactions on the Company's balance sheet as of the transition date is reflected in recording an asset (net of liabilities) for hedging transactions in the amount of \$ 2,552 thousand. In addition the impact of the increase in assets resulted in an increase in deferred income tax liability, net in the amount of \$1,009 thousand. The effect on the statement of income for the six month period ended June 30, 2007 resulted in a decrease in income before taxes in the amount of \$3,450 thousand (mainly an increase in financing expenses in the amount of \$2,377 thousand).

4) Minority interests

Under Israeli GAAP, minority interests are recorded in the balance sheet as a quasi equity item, while under IFRS, minority interests are recorded as part of shareholders' equity. As a result, on transition, minority interests were reclassified in the amount of \$7,535 thousand under a separate item in the shareholders' equity.

Accordingly, in the statement of income, under Israeli GAAP the part of minority interests in the results of the subsidiaries is included as part of the results of the operations. Conversely, under IFRS, the minority interest is not part of the statement of income, and is presented as part of the distribution of earnings among the shareholders. Accordingly, the minority interest for the six month period ended June 30, 2007, amounting to \$4,570 thousand, is not presented as part of the results of operations for the period.

5) Rights in land leased from the Israel Lands Administration

Under leasing agreements with the Israel Lands Administration, the subsidiaries were granted land leasing rights for 49 years (with options for extension), which are due to expire in different periods. Under the leasing agreements, the Company does not have the right to acquire the full rights in the land, and in some cases, the subsidiaries were not granted rights to extend the leasing period.

Under Israeli GAAP, amounts paid for leasing rights were recorded as land as part of the Group's fixed assets. The amount paid was depreciated over the leasing period.

Under IAS 17, leasing of land that does not include an option for acquisition of the full land rights at the end of the leasing period, will be classified as operating leasing, and leasing fees paid to the Israel Land Administration constitute leasing fees paid in advance. Under IFRS, leasing fees will be recorded as expenses paid in advance for operational leasing and not as part of the fixed assets.

Accordingly, with the transition to IFRS, the balance of leasing fees paid in advance was reclassified from fixed assets to expenses paid in advance for operating leasing in the amount of \$4,614 thousand.

6) Deferred taxes

Under Israeli GAAP, deferred tax assets were classified as current or non-current assets, depending on the classification of the assets in respect of which they were generated. Under IFRS, deferred tax assets are classified as non-current assets, even if their expected realization date is expected to be in the short term. Accordingly, with the transition to IFRS, the balance of short-term deferred taxes in the amount of \$41,441 thousand was reclassified, as of January 1, 2007, from other receivables under current assets to deferred tax balances under non-current assets.

7) Reserves from translation differences of subsidiaries

The Company chose to apply the relief determined in IFRS 1 according to which the entire reserve balance from translation differences of subsidiaries as of the transition date in the amount of \$18,728 thousand may be reclassified to retained earnings.

8) Classification of other income/expenses

According to Israeli GAAP, the consolidated financial statements included profits and losses from sales of fixed assets and actuarial changes, expenses for early retirement and for VAT assessments as other income/expenses and not part of operating income. Under IFRS these items will be included as part of the operating income. The impact of the transition to IFRS on the statement of income for the six months ended June 30, 2007 reflects an increase in revenues amounting to \$409 thousand, an increase in cost of sales of \$1,315 thousand, an increase in administrative and general expenses, selling expenses and R&D expenses amounting to \$1,137 thousand and a decrease in other expenses amounting to \$2,042 thousand.

9) Concession contracts

One of the Company's proportionately consolidated Subsidiaries has a concession contract with Government authorities to construct a desalination plant. As part of the agreement the company will operate the plant and sell the Government water produced in consideration for fixed and variable payments as per the agreement. In accordance with Israeli GAAP (since January 1, 2006) and IFRS, Concession contracts will be recorded in the financial statements a financial asset representing the customer debt, whereas the asset is subject to interest. In accordance with Israeli GAAP the interest determined represents the weighted average cost of capital of the project. In addition the recognition of the financial asset is from when the plant commences operations. In accordance with IFRS (IFRIC 12) the interest rate on the financial asset is to be calculated based on the borrower's risk-free interest rate plus interest reflecting the risk of constructing and operating the plant. In addition the asset is recognized from the commencement of establishment of the plant.

The impact of transition to IFRS for the concession contracts resulted mainly in a decrease in short term and long term financial assets as of December 31, 2006 in the amount of \$1,710 thousand and a reduction in shareholders' equity of \$968 thousand.

The impact of the transition to IFRS on the results of operations for the six months ended June 30, 2007 was not material.

9. Update on the description of the Company's business

An update of specific issues in the Description of the Company's Business in the 2006 Periodic Report is presented below.

- 9.1 **Percolation at a dike at the Dead Sea** (Section 4.1.1 of the periodic report): Salt percolation of one of the dikes of the evaporation ponds of ICL Fertilizers at the Dead Sea has affected the sealed layer of the dike. This created spaces in the body of the dike, and fissures have been found along its length. In certain circumstances, these spaces and/or fissures could jeopardize the integrity of the dike. ICL Fertilizers, relying on consultations with international experts, has taken and is taking various steps to preserve and strengthen the stability of the dike, and monitors it closely in order to identify any developments that could lead to the failure of the dike.

The phenomenon of sinkholes is generated mainly by a lowering of the level of the Dead Sea and is increasing in the Dead Sea area. Most of the sinkholes develop near the northern section of the Dead Sea, where ICL Fertilizers' operations are not significant. Sinkholes have also appeared in the area of the evaporation ponds and in other places in the Dead Sea Works area. Development of a sinkhole under a dike could cause the dike to burst, causing loss of the solutions in the pond. ICL Fertilizers is acting to identify the development of sinkholes in the area of the plant, and to fill them in whenever they appear.

- 9.2 **Rise in the level of Pond 150** (Section 4.1.15(g) of the Periodic Report): On May 13, 2007, the Government decided, that the Ministry of Tourism will coordinate the planning and implementation of interim protections at the Dead Sea, as part of the ongoing activities of the intermediate stage (A/2), which relates to actions for preservation and maintenance of the shore and the hotel area near the Dead Sea, and completion of the feasibility studies of the alternatives for long-term protective measures. For this purpose, and in order to create a budget framework, the government announced that it would transfer NIS 200 million to the Ministry of Tourism. It was also decided to appoint a steering committee for the project, to appoint the Governmental Tourist Company as project manager and to ensure that those involved in the project, will obtain support from entities operating in the area. The government also decided that the project to protect the Dead Sea will be defined as an

infrastructure project of national importance under the Planning and Construction Law, 5725-1965, and that the Ministry of Tourism will prepare a plan for a national infrastructure and submit it to the National Infrastructures Committee, for advancing the planning process. It was also decided that the Minister of Finance will define by regulations the financing arrangements between the various partners for completion of the Dead Sea protective measures, including the way of budgeting it.

In the context of a petition submitted by the Israeli Hotel Association (to the High Court of Justice) and the responses of the Government,² the Tamar Regional Council and the Company, the Government claimed that the time is not yet ripe for addressing the issue of financing (of additional temporary protective measures and of a permanent solution). All the other parties, including the Company, stated that the Government is responsible to finance these protective measures. However, in August 2007, the Government submitted a declaration to the Supreme Court claiming that the Government is not responsible, or at least does not bear the main responsibility for the problem or its solution, and that the issue is rather a "conflict between neighbours", namely between Dead Sea Works and the hotels; nevertheless the Government would continue to try to advance the process. On August 13, 2007, the Supreme Court published its decision, according to which it does not accept the position of the Government, that it acts in this matter on a voluntary basis. The Court stated, that also Dead Sea Works and the hotels have to act to find a solution to the problem. On the operational level, the Court ordered, that the Government shall submit within 60 days an updated time-table, with reference also to the organizational frame, including the establishment of a council engaging employees with dedicated occupation to this matter. .

On August 12, 2007, the Government of Israel decided, as part of the annual economic plan (Arrangements Law) that the Minister of Finance shall enter into negotiations with the Tamar Regional Council, Ein Bokek-Hamei Zohar hotels and with Dead Sea Works, to determine how to split between the parties the financial burden of handling damages caused by the rising water level in the Dead Sea area, and of performing the required studies to examine options for a permanent solution.. It was also decided to amend the Economic Arrangements Law of 2002 and to define how to divide financing of the expenses between the parties to the negotiations. Should the parties fail to reach an agreement by September 10, 2007 in respect of the share of each party in financing, the Minister of Finance will submit a proposal to the Government, how to divide financing costs, which would become part of the Arrangements Law.

The Company, based on the opinion of its legal counsel, believes, that it bears no legal responsibility to finance the protective measures.

In respect of the permanent solution - there are a number of alternative solutions. Each solution, compared to its alternatives, has advantages and disadvantages and each solution bears a different cost of implementation. As per the date of this report, no operational feasibility study has been made in the area of the ponds, which could provide the necessary input for the selection of the preferred solution and an estimate of its cost. Hence, it is impossible, at this point of time, to assume, which permanent solution will be selected and what will be the cost associated with its implementation. There is also no agreement, which parties will participate in the financing of the project and how the cost will be split between the parties. Furthermore Dead Sea Works is of the opinion, that it is not obliged, to participate in the financing of the project. Accordingly, the Company is unable, to provide an estimate of the cost, which it might bear in the future, if at all.

- 9.3 **Price control:** (clause 4.1.15 (d) (1) of the Periodic Report): The price of phosphoric acid used in agriculture (green acid) on the local market in Israel is controlled by the Control of Prices of Commodities and Services Law (5756-1996). The scope of green acid sales by ICL Fertilizers in Israel is not significant for ICL.
- 9.4 **Legal proceedings in connection with the Kishon stream** (Section 4.1.16(a) E(2) of the Periodic Report): The Haifa Rowing Club Association filed a class action in the Haifa Magistrate's Court under the Prevention of Environmental Hazards Law (Civil Claims), 5752-1992]. against a number of factories along the banks of the Kishon stream, including against Fertilizers & Chemicals Ltd. (FCL), a subsidiary of the ICL Fertilizers segment. The Government, Municipalities and dozens of factories were included as third parties in the claim. The claim was suing for termination of the flow of effluents into the Kishon, and an order to rehabilitate the stream and restore it to its original condition. On March 29, 2007 the court dismissed the claim outright and allowed the authorities to exercise their discretion in connection with the rehabilitation of the Kishon, noting the practical steps taken by the authorities and the defendants to improve the condition of the Kishon and the considerable

² The government submitted the response to the Supreme Court before the above mentioned government decision of December 12, 2006

improvement in recent years in the quality and condition of the stream's water. In its ruling, the court also mentioned FCL's compliance with the flow permits granted to it, and the constant monitoring of effluents, which have revealed no deviations. On May 21, 2007, the Association appealed the ruling to the District Court of Haifa. This type of class action is virtually without precedent in Israel, in the absence of a Supreme Court ruling of the interpretations or application of the law on which the claim is based, and therefore it is clearly difficult to assess the chances of the petition, considering that the stages of hearing and submission of evidence have not yet been exhausted. In the opinion of the Company, based on the assessment of its legal advisors, the chances that the appeal, and subsequently the claim, will be accepted, are not high.

- 9.5 **Principal projects carried out by the corporation** (Section 4.1.17(b), 4.1.18 and 4.3.17 of the Periodic Report): ICL Fertilizers currently operates a power station for generating electricity in Sedom, and also purchases electricity from Israel Electric Corporation. On August 31, 2006, Dead Sea Works (DSW), which is part of ICL Fertilizers, received a license to generate electricity using power and heat installations (co-generation) in a total capacity of between 400 and 700 megawatts. The license is conditional upon DSW meeting a series of milestones. On February 28, 2007 DSW announced that it requires, at this stage, a license for a 400-megawatt station. Furthermore, up to 700 megawatt there is currently no solution for an electricity-transporting infrastructure from Sedom to the center of the country, nor is such a solution foreseen within the next few years. Therefore application was submitted for a license for a 400 megawatt-station. On May 1, 2007, DSW was scheduled to comply with a milestone in respect of the regulation for commercial arrangements for supply of natural gas. Since this matter has not yet been resolved at the national level, it was agreed with the Electricity Authority that they would renew the license for DSW and revise the milestones accordingly within the coming weeks, and all in accordance with procedures for other licensed entities facing the same problem with regard to gas. There is still no decision regarding establishment of the power station. At this stage, ICL Fertilizers is examining the option of establishing a power station, starting with construction of a plant with a production capacity of 200 megawatt, which will supply electricity to ICL in Israel, with the option of expanding the plant to 400 megawatt.
- 9.6 **Directives in respect of environment quality** (Section 4.2.14(b) of the Periodic Report): In March and June 2007, three claims were filed in the Beersheba District Court against the State of Israel and Ramat Hovav Industrial Regional Council. Two claims were filed by 73 residents of the dispersed Bedouin community in the northern Negev region. The third claim was filed by nine residents from the Beersheba area. ICL is not being sued in these proceedings. The Ramat Hoval Industrial Council is the local industrial council within whose jurisdiction all the factories in the Ramat Hovav area operate, among them the bromine compounds plant of the ICL Industrial Products segment. The plaintiffs allege that various pollutions in the Ramat Hovav area caused the sicknesses from which they suffer, such as respiratory diseases, miscarriages, congenital defects, cancer, and others. The claims sue for amounts of money in respect of the plaintiffs' treatment expenses, as well as compensation for suffering and distress, and punitive damages. The plaintiffs estimate the total amount of the claims at more than NIS 238 million (about \$55 million).
- 9.7 **Subordination of operations to certain laws – the secondary concession** (Section 4.2.16A (1) of the Periodic Report): In recent years, there have been audits on behalf of the Ministry of Industry, Trade and Employment, relating to payment of royalties. The Company did not receive a copy of the audit findings. The Accountant General at the Ministry of Finance, allegedly based on these audits, claims that DSW paid insufficient royalties, amounting to "hundreds millions of shekels". The Accountant General requires the implementation of the arbitration clause in the concession agreement in respect of these insufficient payments.

DSW is attempting to settle the dispute in an agreement with the Government. Should the parties fail to reach an agreement, the dispute will be submitted for arbitration, under the concession agreement.

As of the report period arbitration has not commenced.

Payment of royalties is specified in the concession, which DSW received from the Government and in the secondary concession given by DSW to the Bromine Company, with Government approval. In the opinion of DSW, based also upon its legal counsel, royalties were paid in accordance with the concessions and calculated based on the same method applied consistently for decades, ever since it was a government company. This method was known to the Government, and the Government did not claim (before these letters were received by the Accountant General) improper calculation or payment of royalties. It should be noted that payment of the royalties was examined a number of times by government authorities, including the State Comptroller, and the appropriateness of the amounts was also confirmed by external accountants. Therefore, in the opinion of DSW, these allegations have no foundation, and no provision was made in the financial statements.

- 9.8 **Benefits and the essence of employment agreements** (Section 5.2 (e) of the Periodic Report): A collective labor agreement of DSW of the ICL Fertilizers segment was in force until September 2006. In the reporting period, a new collective labor agreement was signed, valid until the end of September 2010. Rotem Amfert Negev had a collective agreement, which terminated at the end of April 2007. At the reporting date, no agreement has been reached between the Company and the workers council through negotiations for extending the labor agreement. The Histadrut national labor union declared a labor dispute. At the reporting date, the workers of Rotem impose sanctions, which include blocking raw materials and goods from entering and production from leaving the plants and also reducing production of certain plants. Subsequently, some production plants have been shut down; the closure of additional sites is possible and also the total shut down of the plant. Dead Sea Bromine of the ICL Industrial Products segment has a collective agreement valid until the end of December 2007. Dead Sea Magnesium has a collective agreement valid until the end of June 2007. At the reporting date, a request was received from the Dead Sea Magnesium workers council to negotiate the agreement. As long as no new agreement is signed, the parties continue to act under the expiring contract. Regarding the negotiations for renewal of the labor agreements, there are sanctions in the companies from time to time.
- 9.9 **Sale of trade receivables as part of a securitization transaction** (clause 5.43 of the Periodic Report). In July 2007 the facility of securitization of trade receivables was increased to \$300 million
- 9.10 **Limitation of use of brominated flame-retardants** (Section 4.16.2(a)2 of the Periodic Report): In various States in the US are currently discussions held by the Houses of Representatives (Senat and Congress) on drafts of legislations in respect of the use of flame redardants. The Senat of California is handling currently a bill, to prohibit the use of brominated and chlorinated flame retardants for furniture, mattresses and bed-ware. According to the assessment of ICL Industrial Products, this legislation if accepted, will not have a material impact on its results.

10. Events during and after the period

- 10.1 On January 28, 2007, the Company's Board of Directors approved a plan for a private issuance, for no consideration, of 12.9 million options exercisable for the Company's shares, to a group of office holders and other senior managers in ICL and its subsidiaries, in and outside of Israel. See Section 5.2E in the section "Description of the Corporation's Business" in the 2006 annual report. On January 28, 2007, 5.4 million options were allocated, from this plan, of which 2.2 million options were granted to the Company's CEO. On March 27, 2007 6.4 million stock options from this plan were allocated. The remainder of the stock options that were not allocated expired on March 28, 2007.
- 10.2 On March 27, 2007, the Company's Board of Directors resolved to distribute the net earnings of the Company for 2006 as a dividend, after taking into account a dividend of \$90 million which was distributed on September 19, 2006, for part of the year's earnings. Accordingly, on April 25, 2007, a dividend of \$283.9 million was distributed (\$283.4 million net, after deduction of the part of a subsidiary).
- On May 28, 2007, the Board of Directors of the Company resolved to distribute a dividend of \$66.8 million (\$66.7 million net, after deduction of the part of a subsidiary), which was distributed on June 18, 2007.
- On August 21 2007, the Board of Directors of the Company resolved to distribute a dividend of \$88.1 million (approx. \$87.9 net, after deduction of the part of a subsidiary), which will be distributed on September 18, 2007.
- 10.3 The Chairman of the Board, Mr. Yossi Rosen, informed the Board of Directors that he intends to resign from his position as chairman as of December 31, 2007 and that the Israel Corp intends to nominate Mr. Nir Gilad as his replacement. On May 28, 2007 the Board of Directors resolved to nominate Mr. Nir Gilad as acting Chairman of the Board.
- 10.4 On August 6, 2007, ICL entered into an agreement with a group of 17 banks in Europe, the USA and Israel. Under the agreement, the banks will grant ICL a loan of \$725 million for a period of five years (bullet repayment on maturity) bearing interest of short-term Libor + 0.45%. The new loan will replace, inter alia, a similar borrowing facility of 2005 for \$250 million at an interest rate of Libor + 0.6% for five years and which will now be repaid ahead of its original maturity.
- 10.5 In accordance with the Board decision and the recommendation of the auditing committee, the term of the internal auditor, CPA Shlomo Ben Shimol of Deloitte, who has served as internal auditor since May 2005, was extended by a period of three years, ending at the end of May 2010.
- 10.6 In July 2007 ICL Fertilizers signed an agreement with an Indian partner to establish an equally-owned joint venture for production and distribution of specialty fertilizers in India, based on ICL Fertilizer's technology. In other joint ventures in China, reported in the previous quarter (clause 8.3 in the

Director's Report for the first quarter of 2007), there is no progress and it is uncertain whether they will materialize.

- 10.7 On August 13, 2007 a transaction was completed between ICL and Supresta Holdings LLC (the Vendor) a holding company of Ripplewood Holdings LLC, for purchase of the equity interests in Supresta Holdings (hereinafter: Supresta), a company registered in Delaware USA, which engages in the manufacture and marketing of fire retardants and other phosphorus - based products.

ICL paid US \$ 353 million, subject to certain adjustments mainly in respect of working capital according to a mechanism defined in the purchase agreement. The purchase price was paid in cash upon closing of the transaction.

Supresta is the world leader in the manufacture and marketing of phosphorus-based fire retardants. Supresta was established in 2004 when the Vendor acquired the operations from Akzo Nobel and employs more than 300 workers. Supresta owns two factories in the US and in Germany. Supresta has more than 80 phosphorus-based products, which, are used as fire retardants for polyurethanes and engineering resins, plasticizers for the plastics industry as well as functional fluids for powers stations and other uses.

The price was determined by negotiations after a private offer by the Vendor to several potential buyers. ICL will finance the acquisition from its cash-flow and from bank credit. ICL does not anticipate that substantial additional investment in Supresta will be required following the acquisition.

ICL intends to integrate Supresta into its ICL Industrial Products segment to realize operational and other synergies, including purchase of raw materials. This integration will expand the fire retardant product range by the adding polyurethane and engineering resin products.

Main financial figures of Supresta in accordance with the statements received:

(Millions of \$) **	1-6/2007	1-6/2006	2006	2005
Revenues	134.5	130.9	248.8	248.8
Gross profit	25.3	23.3	49.8	53.3
Operational profit	6.0	3.5	7.5	12.6
Adjusted operation earnings *	13.5	11.7	28.9	30.1
Adjusted EBITDA *	18.1	15.6	35.5	37.6
Total assets	281.2	302.3	295.9	317.7

* After writing off non-recurring costs such as management fees, and costs of transfer of assets and revocation of the increase of amortization as a result of the purchase of Supresta by the Vendor in 2004.

** The net profit is not shown because the rights purchased are in a limited liability company that is not regarded as a separate entity for federal tax purposes.

The annual figures are taken from audited statements prepared under US GAAP. The figures for the January-June period have been taken from the monthly statements of the management, un-reviewed and un-audited and not necessarily prepared under GAAP.

The Board of Directors of ICL wishes to thank ICL's management, as well as the employees and managers of the various companies, for their dedicated and skilled contribution to the development of ICL and the achievement of its business results.

Date: August 21, 2007

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Yossi Rosen
 Chairman of the Board

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Akiva Mozes
 CEO