ICL-ISRAEL CHEMICALS LTD. כימיקלים לישראל בע"מ

Directors Report on the State of the Company's Affairs for the period ended September 30, 2006

Following is the Israel Chemicals Ltd. (**"ICL"** or "**the Company"**) Directors Report for the period ended September 30, 2006.

1. Description of the Company and its Business Environment

1.1 Description of the ICL Group

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

ICL's operations are based mainly on the natural resources – potash, bromine, magnesium and sodium chloride from the Dead Sea, and phosphates from the Negev Desert, all on the basis of concessions and licenses from the State of Israel. Operations are based as well 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 central position in the potash and bromine markets. Potash is a core component of fertilizers. The bromine serves a wide range of applications, primarily as a flame retardant. ICL's products are used primarily in the areas of agriculture, electronics, food products, oil and gas drilling, water purification and desalination, and in the detergent, paper, cosmetics, pharmaceutical, automotive and aluminum industries. The ICL Group has decades of accumulated experience in most of its businesses.

The ICL Group 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 the ICL Group by the State of Israel for 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 that are 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.

The ICL Group's main production facilities are based in Israel, Germany, the United States, Holland, Spain, England, China, Brazil and France. Furthermore, the ICL Group has production facilities in Austria, Belgium, Turkey, Argentina, and Australia.

The overseas operations of ICL Group 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 integrated to a high degree with one another, in terms of both supply of raw materials and due to the fact that frequently, one facility utilizes by-products of another facility to produce end-products (for example, bromine is produced by utilizing the bromine present in the byproduct streams from the evaporation ponds used to manufacture potash, etc.)

Approximately 6% of ICL's products are sold in Israel. For some of these sales, 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 the ICL Group.

The four 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 potash into various grades and sells it worldwide. In addition, the segment uses a portion of its production of potash to manufacture compound fertilizers.

ICL Fertilizers also mines and processes phosphate rock from open-pit mines in the Negev Desert, and produces sulfuric acid, fertilizer–grade phosphoric acid, phosphate fertilizers, compound fertilizers based primarily on potash and phosphate and specialty fertilizers in Israel. ICL Fertilizers also produces fertilizers in the Netherlands, Germany and Belgium. In addition, ICL Fertilizers produces phosphate-based animal feed additives in Turkey and in Israel. ICL Fertilizers markets its products worldwide, primarily in Europe, Brazil, India, China, and Israel.

B. **ICL Industrial Products** – ICL Industrial Products produces bromine from an end-brine that is created as a by-product of the production process of potash in Sdom as well as bromine-based compounds. ICL Industrial Products is currently the world's leading producer of bromine, producing around 35% of total global production of this product. ICL Industrial Products uses most of the bromine it produces for its own production of bromine compounds in its production facilities in Israel, the Netherlands and China. Additionally, ICL Industrial Products produces various salts, magnesia and chlorine (produced along with caustic soda from electrolysis of salt created as a by-product of potash production and used as a raw material in the segment's production processes). Additionally, ICL Industrial Products produces chlorine-based industrial products in Israel and the United States. ICL Industrial Products markets its products worldwide.

C. **ICL Performance Products** – ICL Performance Products purifies some of the fertilizer-grade phosphoric acid produced by ICL Fertilizers, purchases purified phosphoric acid from other sources and also produces thermal phosphoric acid. The pure acid is used to produce downstream products with high added value – phosphate salts, food additives, hygiene products, phosphorus derivatives and products for preventing the spreading of fires. ICL Performance Products also produces specialty products based on aluminum oxide (alumina) and other raw materials. ICL Performance Products' production takes place mainly in Germany, the United States, Brazil, Israel and China.

D. **ICL Metallurgy** – ICL Metallurgy produces and markets pure magnesium and magnesium alloys. The magnesium production is done in Sdom from carnallite that is extracted (during the potash production process) from the Dead Sea. ICL Metallurgy's magnesium products are used primarily in casting facilities to produce automotive parts and as a component in the aluminum alloy process in the aluminum industry. ICL Metallurgy's operations are conducted through a joint venture between the ICL Group and Volkswagen AG of Germany.

In addition to these segments, other activities in the Group include desalination and land transportation.

Management by segment is performed on a group-wide managerial-functional basis, even when the managerial structure and legal ownership do not fully correspond.

1.2 The business environment and profitability of ICL

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

ICL is taking 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 U.S. dollars and euro. A portion of its operating expenses are in NIS. Therefore, a devaluation of the average exchange rate of the NIS relative to the US dollar has a positive impact on ICL's profitability, and vice-versa. ICL has more revenues than expenses in Euro. Therefore, an appreciation of the exchange rate of the Euro relative to the US dollar has a positive impact on ICL's profitability, and devaluation has a negative impact. ICL hedges against some of these exposures.

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

The negotiations between the potash suppliers and the Chinese customers regarding the price of potash in the framework of the annual agreement for the year 2006, have continued longer than has been usual in recent years. This has led to a cessation of shipments to China by sea. In addition, the decision by other potash consumers to wait and see the outcome of the negotiations with the Chinese, the ongoing weakness in the Brazilian market and the long winter in Europe, led to a significant reduction in potash sales since the beginning of 2006 and to a corresponding increase in potash stocks. These developments have led a number of major potash producers to announce a reduction in production at their plants, in order to adjust production to sales. At the end of July, an agreement was signed with a major customer in China for the sale of potash for the remainder of 2006, at an increased price, and consignments to this customer were renewed. In September, an agreement was signed with the same customer, under which ICL Fertilizers is to supply more than 2 million tons of potash during a period of three years commencing in January 2007, and ending in December 2009. This agreement reflects a 30% increase in the amount of potash, compared with the previous agreement which is to end at the end of 2006. The potash prices will be fixed by the parties at the beginning of each calendar year.

In August and September, ICL Fertilizers signed agreements with principal customers in India for the supply of more than 800,000 tons of potash during the nine-month period from August 2006 until April 2007.

Following a flood that occurred after the balance sheet date in one of the mines run by the Russian Urakali company, Uralkali was forced to shut down the mine which had had a production capacity of approximately 1.5 million tons of potash, according to public sources, and which had, prior to the flood, an annual output of approximately 1.2 million tons.

The recovery in the electronics market has led to growth in the demand for flame-retardants compared with last year. Sales prices of bromine and many of its compounds rose compared with the corresponding period last year.

ICL Performance Products' operations are affected by increased competition in some of its target markets and by the effects of Euro exchange rates against the Dollar. The purchase in November 2005 of the assets and operations of Astaris in the United States placed ICL Performance Products as a leading player in the fields of specialty phosphate salts.

The rise in energy prices and the drop in the demand for magnesium in some markets negatively impacted the profitability of ICL Metallurgy. The rise in the prices of energy and some raw materials, had an adverse impact on cost of production in other segments as well.

Warfare in the north of Israel had only a marginal effect on ICL.

1.3 This Directors Report accompanies the interim financial statements for the period ended September 30, 2006, and assumes that the reader has those financial statements at his disposal. The Directors Report relates briefly to that period, and assumes that the reader is familiar with the Periodic Report for the year 2005.

2. Results of Operations

2.1 Principal Financial Results

Following is a summary of the results of operations in the reviewed period compared with the corresponding period of last year, in $ millions.

$	1-9/2006		1-9/2005		7-9/2006		7-9/2005		2005	
	$ Millions	% of sales	$ Millions	% of sales	$ Millions	% of sales	$ Millions	% of sales	$ Millions	% of sales
Sales	2,418.5	100.0	2,211.0	100.0	854.3	100.0	727.0	100.0	2,986.0	100.0
Gross profit	842.2	34.8	875.2	39.6	293.3	34.3	300.0	41.3	1,140.7	38.2
Operating income	388.7	16.1	447.8	20.3	128.3	15.0	166.1	22.9	561.3	18.8
Pre-tax income	377.6	15.6	439.0	19.9	132.7	15.5	156.3	21.5	514.3	17.2
Net income	283.7	11.7	340.2	15.4	94.8	11.1	143.7	19.8	422.2	14.1
Cash flow from current operations	259.3	-	338.7	-	121.9	-	95.6	-	490.9	
Investment in property, plant and equipment less grants	93.3	-	112.4	-	30.3	-	37.4	-	147.8	

2.2 Results of operations for the period January – September 2006

Sales

Sales of ICL Group in the reporting period amounted to approximately $2,418.5 million, compared with $2,211.0 million in the corresponding period last year, an increase of approximately 9.4%. This growth reflects mainly the effect of the inclusion of sales in respect of the operations of Astaris (acquired in November 2005), and price rises in most of the segments of operation, which were offset by a quantitative drop in potash sales and of a number of other products.

	1-9/2006		1-9/2005	
	$ Millions	%	$ Millions	%
Israel	151.6	6.3	161.7	7.3
North America	574.5	23.8	242.6	11.0
South America	249.6	10.3	247.4	11.2
Europe	896.3	37.1	946.5	42.8
Asia	458.7	19.0	515.7	23.3
Rest of the World	87.8	3.5	97.1	4.4
Total	2,418.5	100.0	2,211.0	100.0

The breakdown in sales for the first nine months of 2006 shows a sharp increase in sales and in percentage of sales in North America. This growth arises primarily from the addition in sales in the ICL Performance Products segment as a result of the acquisition of the operations of Astaris (in November 2005). In South America, there was a slight increase compared with last year, due to sales stemming from the acquisition of new operations in Brazil (Astaris and Adicon), which were not included last year. In the other markets, sales decreased, due mainly to a decrease in potash sales as a result of the ongoing negotiations between the world's leading potash suppliers and their Chinese customers, which ended at the end of July as stated, due to the impact of the revaluation of the Brazilian Real on the sales of fertilizers in that country, and due the effects of the long winter on the sales of fertilizers in Europe.

Gross Profit

Gross profit totaled $842.2 million, a decrease of 3.8% compared with the same period last year. Gross profit for the period includes payments on account by insurance companies in the sum of approximately $29 million, which were recorded in the first and third quarters, for loss of profit following the flood damages in Sdom at the end of 2004. Last year, compensation was recorded for this damage in the sum of $12.1 million.

The gross profit was affected adversely mainly by the drop in sales quantities of potash and by the growth in the costs of principal inputs, including the rise in energy prices, the prices of some raw materials and land transportation costs. Furthermore, the appreciation of the NIS against the dollar at the end of the period by 6.5% compared to the beginning of the period, brought about an increase in the dollar value of certain non-cash expenses in NIS, namely an expense of approximately $12 million, which derives from an increase in dollar liabilities to employees following appreciation of the shekel. Last year the NIS depreciated by 6.7% at the end of the reporting period compared to its beginning and created a non-cash income of a similar amount. Despite these adverse factors, , the rise in sales prices, as aforesaid, the acquisition of the Astaris activity and the ongoing efficiency measures, partially offset the erosion in gross profit. The improvement in selling prices at ICL Industrial Products resulted in record earnings in the segment in the first nine months of the year.

Gross profit out of sales turnover is 34.8%, compared with 39.6% in the same period last year. The reduction in gross profit was influenced mainly by a reduction in the quantities of potash sold. Furthermore, profit margins of Astaris are lower than the Company's average.

Sales and marketing expenses

Sales and marketing expenses totaled NIS 337.2 million, an increase of 3.1% compared with the corresponding period last year. The increase in expenses stems from the consolidation of new operations acquired in the United States and Brazil, which did not belong to the Company last year. Despite the negative effect of the rise in energy prices on transportation costs in general, the marine transportation costs in the ICL Fertilizers segment dropped, compared with the corresponding period last year. This is the result of a drop in bulk marine transportation costs compared with the prices that prevailed in the corresponding period of last year and a drop in the quantities conveyed. It is noted that during the third quarter of the year, marine transportation prices started to rise.

General and administrative expenses

General and administrative expenses totaled $90.3 million, an increase of approximately 17.0% compared with the corresponding period last year. The increase in administrative expenses stems mainly from the consolidation of the operations acquired in the United States and Brazil.

Research and development expenses

R&D expenses (net of grants from the Chief Scientist) amounted to approximately $26.0 million, an increase of about $2.9 million compared with the same period last year, stemming mainly from the consolidation of operations acquired in the United States and Brazil.

Operating income

Operating income decreased by 13.2% compared with the corresponding period last year, reaching $388.7 million. This decrease stems mainly from a reduction in gross profit as aforesaid. The percentage of operating income out of turnover came to 16.1% compared with 20.3% last year.

Financing expenses

Net financing expenses amounted to approximately $25.1 million, compared with $3.2 million last year. During the corresponding period last year, the Company had income from exchange rate differentials in the sum of $17 million, compared with $5 million this year. In addition, net financing expenses were influenced by an increase of approximately $111 million in the average balance of net financial liabilities in the period, compared with the corresponding period last year, and by a rise of approximately 1.3% in the average dollar interest rate for the period.

Tax Expenses

The tax expense for the period amounted to $ 105.3 million, compared with $ 99.3 million in the previous year. The pre-tax profit tax rate rose from 22.6% to 27.9%.
The low tax rate during the previous period was due to the fact that, following legislation of an amendment to the Income Tax Ordinance in July 2005, which updated corporate tax rates and provided that corporate tax would drop gradually to a rate of 25%, a reduction in tax expenses on income was recorded in the amount of approximately $29 million.

Other income

Other income includes the sum of $10.5 million for an update of provisions made for employee retirement.

Net income

Net income amounted to $283.7 million, compared with $340.2 million in the same period last year.

2.3 Results of operations for the period July – September 2006

Sales

Sales of ICL Group i the quarter amounted to $854.3 million, compared with $727.0 million last year, an increase of approximately 17.5%.
The increase in sales reflects mainly the inclusion of the sales of the operations acquired from Astaris, and the price rises in most of the Group's segments of operation.

	7-9/2006		7-9/2005	
	$ Millions	%	**$ Millions**	%
Israel	49.7	5.8	50.4	6.9
North America	203.6	23.8	72.8	10.0
South America	121.5	14.2	97.2	13.4
Europe	273.7	32.0	291.3	40.1
Asia	181.8	21.3	177.8	24.5
Rest of the World	24.0	2.9	37.5	5.1
Total	854.3	100.0	727.0	100.0

The breakdown of sales in the quarter is largely similar to that for the period, and reflects the same trends. Total sales to Asia remained the same as in the corresponding quarter last year, despite the halt in sales of potash to China and India during the first half of the year, mainly due to the increase in sales of bromine and bromine compounds, an increase in sales in the ICL Performance Products segment and due to sale of a desalination plant in India by IDE. The month of September, after signing the agreements for sale of potash to China and India, was characterized by a relatively high pace of sales.

Gross profit

Gross profit amounted to $293.3 million, a decrease of 2.2% compared with last year. The gross profit margin decreased from 41.3% to 34.3% of total turnover.

The decrease in the sales of the fertilizer segment and the rise in energy prices and in the prices of some raw materials and also the appreciation of the NIS against the dollar, which increased the dollar value of NIS expenses, resulted in a decrease in gross profit. The average exchange rate of the NIS against the dollar during the current quarter was up by 3.3% compared to the previous quarter, which increased the dollar value of current expenses in NIS. The appreciation during the quarter amounted to 3.1%,, which caused a non-cash expense of approximately $5.5 million, which derives from an increase in dollar liabilities to employees. On the other

hand, price increases in some of the segments set off the decrease in gross profit.
Gross profit for the quarter includes an on-account payment by insurance companies in the sum of approximately $12.7 million for loss of profit following the flood damages in Sdom at the end of 2004. Last year, a similar payment was recorded for this damage in the sum of $12.1 million.

Sales and marketing expenses

These expenses amounted to $125.5 million, an increase of approximately 24.1% compared with the corresponding period last year. This increase in expenses was due mainly to the consolidation of new operations acquired in the United States and Brazil.

General and administrative expenses

These expenses amounted to $30.4 million, an increase of approximately 21.1% compared with the corresponding period last year, mainly due to the acquisition of assets and operations from Astaris.

Research and development expenses

R&D expenses (net of grants from the Chief Scientist) amounted to approximately $9.1 million, an increase of about $1.4 million compared with last year, stemming mainly from consolidation of the operations acquired in the United States and Brazil.

Operating income

Operating income decreased by 22.7% compared with last year, and reached $128.3 million. Operating income out of sales amounted to 15.0%, compared with 22.9% last year.

Financing expenses

Financing expenses amounted to $6.6 million, compared with income of $4.4 million last year, an increase of $2.2 million. Financing expenses were influenced by an increase of approximately $153 million in the average balance of net financial liabilities compared with the corresponding quarter last year, and by a rise of approximately 1.3% in the average dollar interest rate for the period.

Other income

Other income includes the sum of $10.5 million for an update of provisions made for employee retirement.

Income tax

Income tax expenses in the reported period amounted to $42.5 million, which is approximately 32.1% of pre-tax income, compared with about 8% last year. The low tax rate during the previous period was due to the fact that, following legislation of an amendment to the Income Tax Ordinance in July 2005, which updated corporate tax rates and provided that corporate tax would drop gradually to a rate of 25%, a reduction in tax expenses on income was recorded in the amount of approximately $29 million.

Net income

Net income for the quarter amounted to $94.8 million, compared with $143.7 million in the corresponding period last year.

3. Segments of Operation

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

Sales CIF By segment	1-9/2006		1-9/2005		**7-9/2006**		**7-9/2005**	
	$ Millions	**% of total sales**	**$ Millions**	**% of total sales**	**$ Millions**	**% of total sales**	**$ Millions**	**% of total sales**
ICL Fertilizers	1,032.1	39.7	1,207.4	50.4	392.4	42.8	397.9	50.3
ICL Industrial Products	663.8	25.5	574.9	24.0	195.5	21.3	194.0	24.5
ICL Performance Products	776.5	29.8	471.0	19.6	279.0	30.4	154.7	19.6
ICL Metallurgy	67.7	2.6	81.4	3.4	22.5	2.5	23.5	3.0
Other and setoffs	(121.6)		(123.7)		(35.1)		(43.1)	
Total	2,418.5		2,211.0		854.3		727.0	

Note: Sales data in the segments and their percentages out of total sales, are before setoff of inter-segment sales.

Operating income By segment	1-9/2006		**1-9/2005**		**7-9/2006**		**7-9/2005**	
	$ Millions	**& of segment sales**	**$ Millions**	**& of segment sales**	**$ Millions**	**& of segment sales**	**$ Millions**	**& of segment sales**
ICL Fertilizers	161.3	15.6	277.1	22.9	60.8	15.5	108.2	27.2
ICL Industrial Products	177.9	26.8	110.3	19.2	46.7	23.9	41.4	21.4
ICL Performance Products	68.9	8.9	50.1	10.6	27.0	9.7	14.0	9.1
ICL Metallurgy	(26.7)	(39.5)	0.6	0.7	(10.7)	(47.6)	(0.8)	(3.6)
Other	7.3		9.7		4.5		3.3	
Operating profit (consolidated)	388.7	16.1	447.8	20.3	128.3	15.0	166.1	22.9

Note: The profit percentage is out of sales before setoff of inter-segment sales.

3.1 ICL Fertilizers

Sales

The volume of sales in the segment in the reporting period amounted to approximately $1,032.1 million, a decrease of 14.5% compared with the same period last year. The decrease in sales turnover arises mainly from a sharp drop in potash sales, mainly to China and India, which was partly offset by a price rise in sales of green acid, phosphates and phosphate fertilizers.

Profitability

Operating income in the segment amounted to $161.3 million, a decrease of approximately 41.8% compared with the corresponding period last year. The operating margin on sales was 15.6%, compared with 22.9% in the corresponding period last year.

The decrease in profit stems from smaller quantities of potash sold, a rise in main production input costs, and a number of production problems at certain plants, which caused output decreases in Europe, which was partly offset by operating improvements in the phosphate sub-segment and a reduction in prices of sulfur, an input for some ICL production sites. The operating profit was also adversely affected by an appreciation of the exchange rate of the shekel compared with the dollar. The operating income includes revenues from insurance payments received, recorded in this quarter and in the first quarter of the year in respect of loss of profits following flood damage at Sdom at the end of 2004.

The average prices of bulk transportation went down in comparison with last year. Conversely, the average cost of land transportation rose in comparison with last year, mainly as a result of the increase in the cost of truck transportation due to increased prices of diesel fuel and a revision of rail transportation prices. In the third quarter, there was an increase in average sea transportation prices compared with the corresponding period last year, and compared with the first half of this year.

Potash

Potash – Sales Revenue and Income

$ Millions	1-9/2006	1-9/2005	7-9/2006	7-9/2005	2005
Income*	623.9	817.0	232.5	269.9	1,064.1
Operating income	145.8	261.8	52.1	107.7	333.6

* including revenue from inter-segment sales.

The decrease in revenue compared with last year is the result of a decrease in quantities sold, which was partly offset by the price rises. The decrease in sales stems from the drop in the demand for potash, due to the wait for the closing of the contract for the sale of potash to China, which was signed only in July, and due to the weak markets in Europe and Brazil.

At the end of July, an agreement was signed with a major customer in China for the sale of potash for the remainder of 2006, at an increased price, and consignments to this customer were renewed. In September, an agreement was signed with the same customer, under which ICL Fertilizers is to supply more than 2 million tons of potash during a period of three years commencing in January 2007, and ending in December 2009. This agreement reflects a 30% increase in the amount of potash, compared with the previous agreement which is to end at the end of 2006. The potash prices will be fixed by the parties at the beginning of each calendar year.

In August and September, ICL Fertilizers signed agreements with principal customers in India for the supply of more than 800,000 tons of potash during the nine-month period from August 2006 until April 2007.

The 44.3% drop in operating income derives primarily from the considerable drop in quantities sold; in addition, there was a switch of sales from the

Israeli plant, where the profitability is relatively high, to the mines of ICL in Europe; also the rise in the prices of some production inputs, a number of faults which caused a drop in production in Europe and the impact of the appreciation of the shekel against the dollar, contributed to the lower operating income.

Potash – Production and Sales

Thousands of tons	**1-9/2006**	1-9/2005	**7-9/2006**	7-9/2005	**2005**
Production	3,671	3,935	1,171	1,299	5,263
Sales to external customers	2,577	3,660	999	1,185	4,721
Sales to internal customers	168	194	53	67	252
Total sales (including internal sales)	2,745	3,854	1,052	1,252	4,973

The decrease in potash production stemmed partly from a stoppage of several days for maintenance operations at the Sdom plant, from a fall in production in Europe and from closure of the Suria mine in Spain, as planned.

ICL Fertilizers is looking into a variety of ways of continuing reorganization of its mining operations in Europe.

The decrease in sales stems mainly from lack of sales to China and India, and from a fall in sales to Brazil and Europe.

Brine percolation exists at one of the dikes of the evaporation ponds of ICL Fertilizers at the Dead Sea. In consultation with international experts, ICL Fertilizers has taken and is taking various maintenance actions to preserve the stability of the dike.

Fertilizers and Phosphates

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

Fertilizers and Phosphates – Sales Revenue and Income

$ Millions	**1-9/2006**	**1-9/2005**	**7-9/2006**	**7-9/2005**	**2005**
Income*	436.8	419.9	168.9	139.1	548.5
Operating income	14.1	15.2	7.8	0.8	15.4

* including revenue from inter-segment sales.

Revenue in the period was approximately 4.0% higher than in the corresponding period last year, mainly due to a rise in sales of green acid and phosphate rock to external customers.

The decrease in operating income in the period stemmed mainly from the decrease in revenue and from the rise in the prices of energy inputs, and from the appreciation of the shekel compared with the dollar, as set out above. On the other hand, the positive income was influenced by operational efficiency in production as a result of implementation of the strategic plan at Rotem.

Implementation of the strategic plan, together with an increase in sales resulting also from an increase in prices, brought about an improvement in operating profit for the quarter, compared with the corresponding quarter last year. This improvement occurred, despite the negative impact of the appreciation of the shekel against the dollar as set out above.

Fertilizers and Phosphates – Production and Sales

Thousands of tons	1-9/2006	1-9/2005	7-9/2006	7-9/2005	2005
Phosphate ro					
Production	2,262	2,551	742	839	3,236
Sales*	327	296	69	108	365
Fertilizers					
Production	1,191	1,237	421	407	1,636
Sales*	1,286	1,267	529	454	1,671

* To external customers.

Phosphate rock is produced according to demand, both for internal uses and for sales to external customers, while maintaining suitable stock levels. The drop in production compared with the corresponding quarter last year stemmed, among other things, from the strategic change in the use of various types of rock, in which the operation of the calcining facility at the Zin site in the Negev was ceased. It should be noted, that during the course of the year, production of fertilizer-grade phosphoric acid (green acid) improved considerably as a result of enhanced processes.

The running-in process of the plant at Mishor Rotem for the production of technical grade mono-ammonium phosphate (MAP) has been completed, and the current output is being sold.

3.2 ICL Industrial Products

Sales:

Operations in this segment in the report period amounted to approximately $663.8 million, an increase of about 15.5% compared with last year. The increase in sales derives mainly from price rises in almost all areas of the segment's operations, and from an increase in the quantities sold of some products, particularly flame retardants and biocides for water treatment.

The increase in sales revenue from flame retardants was mainly the result of price rises in most of the products and increased quantities sold in comparison with the same period last year, as a result of the recovery in the demand for flame retardants.

Sales revenue from inorganic bromine products increased, due to price rises and despite the drop in quantities sold.

Revenues and profitability from sales of agricultural products decreased, mainly due to the smaller quantities sold of methyl bromide approved for "critical uses", as prescribed in the Montreal Protocol.

A significant increase in sales and profitability occurred in water treatment biocides as a result of a growth in sales quantities following a new agreement with a retail distributor, and as a result of price rises in the main target market (North America).

Revenues for magnesia products were similar to last year, with price rises and changes in sales mixes being offset by a reduction in quantities sold (mainly due to a reduction in magnesium sales for the refractory industry).

Revenue from sales of Dead Sea salts increased slightly compared with last year.

Profitability

Operating income in this segment in the report period amounted to approximately $177.9 million, an increase of about 61.3% compared with last year.

The increase stemmed mainly from an increase in selling prices and from a decrease in the prices of some of the raw materials, which was partly offset by increased expenses for energy and other inputs. The operating profit was also adversely affected by an appreciation of the exchange rate of the shekel compared with the dollar.

With the trend in the European Union to consider limiting the use of bromine-based flame retardants, European Union authorities instituted a process of risk assessment of the currently used bromine-based flame retardant – DECA. This product contains about 97% pure DECA, and the remainder is a substance called NONA. In its decision of October 13, 2005, which is based on that risk assessment process, the European Union Council announced that DECA had been removed from the list of substances banned under its Restriction of Hazardous Substances (RoHS) directive. Recently, EU authorities have voiced the opinion that the above decision referred only to pure DECA, without any added NONA. ICL Industrial Products acts through a forum, where all big producers of DECA are represented, to convince the EU authorities, not to limit the use of DECA, which contains NONA, for certain applications. In addition, ICL Industrial Products is taking legal steps against the above decision, due to the fact that the EU authorities are not prepared to alter their position. On August 24, 2006, the government of Sweden announced a prohibition of use of DECA for textile products, furniture and cables, which shall come into effect on January 1, 2007. England and France objected to the Swedish legislation. The European Market Commission has announced that in its opinion, the prohibition contravenes the laws of the common market [and therefore, the matter will be referred to the European court].

In Europe, a regulatory process is currently taking place to assessing the dangers of HBCD flame retardants. A discussion of the assessment will take place in December 2006. The process of assessing the health risks of the flame retardant called "TBBA" in Europe ended with a positive assessment, no risk being identified to employees or the public at large. The environmental risk assessment for TBBA is still ongoing, and the results are expected in the first quarter of 2007.

3.3 ICL Performance Products

After purchase of the assets and operations of Astaris in the U.S. and the Adicor plant in Brazil, ICL commenced organizational actions intended to integrate the purchased operations with existing operations at ICL Performance Products in order to maximize the synergy between the operations. As part of this process, in September 2006, Mr. Richard V. Kennedy, Jr. was appointed as CEO for ICL Performance Products, as were managers for the geographical units and the areas of operation within the segment.

Sales

Sales in the segment totaled $ 776.5 million, an increase of 64.9% compared with the corresponding period last year. The growth in turnover compared with the corresponding quarter last year stems from inclusion of the activity acquired from Astaris in November 2005, an increase in some sales prices, a quantitative growth in some of the segment's product lines, and the acquisition of Adicor, which manufactures additives for the food industry in Brazil.

On the other hand, surplus production for the segment's products in some of its markets and the increasing competition in some of its target markets, which led to a quantitative decrease in some products, is still impeding growth in some of the segment's areas of activity.

Profitability

Operating income in this segment in the report period totaled $68.9, which is 37.6% higher than in the corresponding period of last year. The operating margin on sales was 8.9%, compared with 10.6% in the corresponding period last year. The drop in profitability stems mainly from the consolidation of the operations of ICL Performance Products in America (purchased from Astaris) with its relatively lower profitability rates than those of ICL Performance Products in Europe.

The growth in revenues, as stated, coupled with an operational improvement in some activities, the consolidation of the results of the operations acquired in America and further efficiency and savings activities, contributed to the increase in profit. The increase was partly offset by an increase in main production input costs, and by a rise in the prices of raw material and energy.

3.4 ICL Metallurgy

Sales

Sales in this segment amounted to $67.7 million, a decrease of about 16.8% compared with last year.

The drop in sales stemmed mainly from a drop in sales prices of the various types of magnesium, mainly influenced by the slowdown in the automotive industry in North America, and an increase in competition from Chinese manufacturers in Europe. On the other hand, there was a slight increase in sales quantities of various kinds of magnesium.

Profitability

The operating loss in the segment totaled approximately $26.7 million, compared with an operating profit of $0.6million in the corresponding period last year. The loss stems from a decrease in selling prices, as stated, and a rise in energy input prices, as well as a decrease in production quantities during the period.

After the end of the quarter, the US government announced that protective customs duties imposed upon the import of magnesium from China into the USA by a particular Chinese exporter would be cancelled. The Western magnesium manufacturer Norsk Hydro (NH) announced that it had decided to cease manufacture of magnesium at its Canadian plant, starting in mid – 2007. The impact of these events on the market – on the one hand, a possible increase in supply of products from China to the USA, and on the other hand, a reduction in supply in North America, due to the cessation of NH's production – is not yet clear.

4. The financial position and financial resources of the Group

ICL's policy is to diversify its sources of financing among various financial instruments and between local and foreign sources.

In the first nine months of the year, the net financial liabilities of the Group remained stable in comparison with the balance at the end of 2005. At the end of the period those liabilities amounted to $598.4 million. This stability is the result of a strong cash-flow, which served however a dividend payment of $180 million. Net financial liabilities including securitization and discounting of trade receivables decreased by $32 million during the reporting period.

The Group's principal sources of financing are short-term and long-term bank loans, from banks in Israel and from international banks.

Cash flow

ICL's cash flow from operating activities in the first nine months of 2006 amounted to $259.3 million, compared with $338.7 million in the same period last year, a decrease of approximately $79.4 million. The decrease in potash sales in the fertilizers segment was partly offset by a reduction in customer debt, but led to growth in potash stocks. Tax payments in cash also contributed to the decrease in cash flow from operating activities. Cash-flow from operating activities during the third quarter amounted to $121.9 million, up by $26.3 million compared to the same period last year. Cash flow from operating activity was the main source of financing for investments in fixed assets in an amount of $93.3 million, and for payment of a dividend of approximately $180 million.

Insurance

In April 2006, ICL Group increased its property insurance against physical damage and loss of profits due to earthquake, from $500 million to $575 million, at market terms for this type of cover.

5. Investments

In the report period, investments in property, plant and equipment net of investment grants amounted to approximately NIS 93.3 million, compared with investments in property, plant and equipment net of grants amounting to approximately $112.4 million last year.

6. Manpower

The total number of employees at ICL Group as at September 30, 2006 is 9,470, compared with 8,809 on September 30, 2005. The increase in the number of employees compared with the corresponding period last year is mainly in the ICL Performance Products segment, due to the acquisition of the operations of Astaris in the United States and Brazil and an increase in operations in China.

7. Exposure to market risks and their management

No material change occurred during the report period, compared with the Directors' Report for 2005.

8. Update of the description of the corporation's business

No material change occurred during the report period, compared with the Directors' Report for 2005, except as set out below:

8.1. Update regarding increased level of pool 150

(Section 4.1.14 F of the Chapter on Description of the Corporation's Business);

In March 2006, a petition was filed with the High Court of Justice by the Hotels Union against the State of Israel and others, including Dead Sea Works from ICL Fertilizers. The remedies sought under the petition are to require the State of Israel: (1) to decide to adopt a permanent solution regarding the lagoon alternative or the salt harvest alternative (described in the description of the corporation's business, mentioned above), and disqualifying the alternative under which the hotels would be relocated; and (2) to complete by the end of 2007 a permanent solution to be selected. In addition, a remedy prescribing that the hotels are not required to take part in the cost of the permanent solution is also sought. Likewise, an interim order prohibiting increase of the water level of the pool above 609.5 m is also sought. The Supreme Court has ruled not to issue an interim order as yet.

Pursuant to a long list of decisions by the State of Israel and by Committees on its behalf in this regard, a decision was made in September 2006 by the Ministerial Committee on Society and Economics (the Socio-Economic Cabinet) to once again delegate the responsibility for handling this matter on the Minister of Tourism. The Minister is required to submit a recommendation to the government by the end of 2007, regarding preparations required for solving the long-term protection of the Dead Sea coastline. The Minister of Tourism has also been asked to examine methods for implementing an interim solution to protect the coastline of the Dead Sea.

In a hearing held in September 2006, the Supreme Court required the Government to submit a detailed supplementary report relating to the timetable for the future operations that it is required to take. The Supreme Court noted that it wishes to assume that, as a result of the aforesaid government decision, treatment of interim solutions and of the decision regarding the permanent solution will be speeded up, the responsibility for such being upon the steering committee headed by a representative of the Ministry of Tourism.

8.2. Update regarding legislative processes in the European Union

(Sections 4.1.14(i), 4.2.15(c)(5), 4.3.15(c)).

A draft of the framework statute for registration and evaluation of chemicals in the EU (known as REACH) has passed first reading in the European Parliament. The bill is expected to be submitted for second reading in the Parliament in December 2006, and to come into force, if approved, in April 2007. It is expected that this legislation shall come into force immediately upon publication, in all EU countries. The legislation, if passed, will apply to chemicals currently on the market, and to new chemicals manufactured in and/or imported into EU countries, in quantities of more than one ton per year.

In October 2006, the EU Parliamentary Committee on the Environment approved an amendment to the bill which requires that manufacturers of materials that undergo authorization under the law to effect a socio-economic assessment of all uses, so as to prove that the advantages of use are greater than the risks.

9. Events during and after the period

9.1 At the Annual General Meeting of Shareholders of the Company, which took place on April 23, 2006, it was decided, inter alia, to reappoint Messrs. Yossi Rosen, Irit Izakson, Chaim Erez, Muhammad Dahleh, Moshe Vidman, Noga Yatziv, Avisar Paz, Gilad Shavit, Amnon Sadeh and Avraham (Beiga) Shochat as Company Directors. The appointment of Messrs. Yaacov Dior and Ben Rabinovitz as outside directors remains in effect. On May 9, 2006, Mr. Gilad Shavit ceased to serve as a Company Director. On May 28, Mr. Nir Gilad was appointed to serve as a Company Director. On August 31, 2006, Mr. Ben Rabinovitz, an External Director, and Adv. Muhammad Dahleh ceased to serve as a Company Directors. On September 5, 2006, the general meeting resolved to appoint Prof. Yair Urgeler as an External Company Director, Mr. Victor Medina as a Company Director and to extend the appointment of Mr. Yaacov Dior as an External Company Director for an additional term.

9.2 Mr. Asher Rappaport, VP of ICL was appointed, as of November 1, 2006, to act as VP Human Resources at ICL. Mr. Dan Mesika, CEO of Dead Sea Magnesium Ltd. (DSM), of ICL Metallurgy, gave notice of his resignation, in force as of December 31, 2006, and Mr. Arieh Sodak was appointed in his place as CEO of DSM, effective January 1, 2007.

9.3 On March 27, 2006 the Board of Directors of the Company approved an incentive plan in which 700,000 ordinary shares of the Company were allotted to senior executives at the Company and at the companies under its control. The shares were allotted free of charge to a trustee, and are blocked for one year from the date of allotment.

9.4 On May 9, 2006, and on September 19, 2006, the Company paid a cash dividend. The total amount paid is $180 million.

9.5 On September 18, 2006, a subsidiary of I.D.E. Technologies Ltd. ("IDE") (Desalination Engineering), received notice from the Government of Israel that it had won a tender regarding the BOT design, financing, erection and operation of a desalination facility near Hadera, for the treatment of about 100 million cubic meters of sea water per year. The shareholders of the subsidiary are IDE and Housing and Construction Holdings Ltd., in equal shares. ICL holds 50% of IDE.

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.

November 21, 2006

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Akiva Mozes, CEO	**Yossi Rosen** **Chairman of the Board**