Directors Report on the State of the Company's Affairs for the period ended June 30, 2005

1. Description of the Company and its Business Environment

1.1 Description of the ICL Group

Israel Chemicals[1] **("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 primarily on natural resources – potash, bromine, magnesium and sodium chloride from the Dead Sea, and phosphates from the Negev Desert, all on the basis of concessions from the State of Israel. Operations are based as well on potash and salt mines in England and Spain under leases and concessions 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, Holland, Spain, England, the United States, China and France. Furthermore, the ICL Group has production facilities in Austria, Belgium, Turkey, Brazil, 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. More than 92% of ICL's products are sold outside Israel.

Less than 8% of its products are sold in Israel. For some of these products, ICL has been declared a monopoly in Israel. Approximately 45% of ICL's sales revenue stems from manufacturing operations outside Israel.

The segments of operation

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 segments of ICL's operations are grouped according to managerial-functional considerations. There is no full correlation between the managerial and the legal structure.

Following is a description of the business segments:

[1] In this document, "ICL Group" means Israel Chemicals Ltd. and its consolidated companies.

a. ICL Fertilizers – ICL Fertilizers produces potash from the Dead Sea and extracts 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 mines and processes phosphate rock from open-pit mines in the Negev Desert, and produces in Israel sulfuric acid, fertilizer–grade phosphoric acid, phosphate fertilizers, compound fertilizers based primarily on potash and phosphate and specialty fertilizers. ICL Fertilizers also produces fertilizers in Holland, Germany and Belgium. In addition, ICL Fertilizers produces phosphate-based animal feed supplements 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 and bromine-based compounds. ICL Industrial Products is currently the world's leading producer of bromine, producing about one third of total global production. ICL Industrial Products uses approximately 80% of the bromine it produces for its own production of bromine compounds in its production facilities in Israel, Holland and China. Additionally, ICL Industrial Products produces salt, magnesia and chlorine (from electrolysis of salt created as a by-product of potash production), as well as chlorine-based industrial products in Israel and the United States.
   ICL Industrial Products markets its products worldwide.

c. ICL Performance Products - ICL Performance Products processes some of the fertilizer-grade phosphoric acid produced by ICL Fertilizers and uses it to produce downstream products with high added value. These products include food-grade phosphoric acid, phosphate salts, food additives and hygiene products. ICL Performance Products also produces specialty products based on aluminum oxide (alumina) and other raw materials. The lion's share of ICL Performance Products' production takes place at facilities in Europe and specifically in Germany, as well as Israel, China and other countries. The products based on specialty phosphates represent approximately two-thirds of ICL Performance Products' sales.

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, ICL has other operations that include water desalination (via a company that is 50% owned by ICL – IDE Desalination Engineering Ltd.) and land transportation (by the subsidiary Mifalei Tovala Ltd. – hereinafter "Mifalei Tovala").

   Israel Corporation Ltd. ("Israel Corporation") holds approximately 50.12% of the share capital and voting rights (about 49.37% at full dilution[2]) of Israel Chemicals Ltd. ("the Company") The Ofer Group is the controlling shareholder in Israel Corporation.

[2] Assuming that all the debentures and all the options for shares of the Company will be converted to shares.

1.2 The Business Environment 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 the global economic situation.

ICL is taking steps to adjust its marketing and production policy to the circumstances in world markets by 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 the euro, while about one quarter of costs are in shekels. Consequently, devaluation in the dollar-shekel exchange rate has a positive effect on ICL's profitability, and the opposite is true for appreciation. ICL has surplus income over expenses in euro, so that appreciation of the euro-dollar exchange rate has a positive effect on ICL's profitability, and the opposite is true for devaluation. ICL customarily hedges against part of this exposure.

The Group's loans usually bear variable interest, a fact which exposes the Group to changes in the interest rates. The group hedges part of this exposure by means of financial instruments, including derivatives.

During the Report Period, prices continued to rise in most of ICL's areas of operation, due mainly to global economic growth and improvement in the Group's target markets. Basic conditions in the world agricultural market, which affect the demand for fertilizers, continue to be good.

The demand for elementary bromine and some of ICL Group's bromine-based products, particularly clear brines for oil and gas drilling, also increased as a result of improvement in the target markets, although in some of the markets, notably electronics, the demand has slowed somewhat.

Price rises at ICL Performance Products had a positive effect on the segment's results, despite the ongoing economic slowdown in Europe, the segment's main market, and the appreciation of the euro exchange rate, which made those of the segment's products manufactured in Europe less competitive.

1.3 This Directors Report accompanies the interim financial statements for the period ended June 30, 2005, 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 2004.

2. Results of Operations

2.1 Principal Financial Results

	1-6/2005		1-6/2004		4-6/2005		4-6/2004		2004	
	$ millions	% of sales	$ millions	% of sales	$ millions	% of sales	$ millions	% of sales	$ millions	% of sales
Sales	1,484.0	100.0	1,290.6	100.0	773.9	100.0	671.5	100.0	2,715.0	100.0
Gross profit	575.2	38.8	432.3	33.5	296.1	38.3	231.9	34.5	937.1	34.5
Operating income	281.7	19.0	151.4	11.7	142.2	18.4	90.3	13.5	354.4	13.1
Pre-tax income	282.7	19.0	133.3	10.3	145.6	18.8	80.9	12.1	309.5	11.4
Net income	196.5	13.2	106.9	8.3	101.2	13.1	74.6	11.1	250.5	9.2
Cash flow from current operations	243.1		205.5		119.0		114.3		429.9	
Investments in property, plant and equipment less grants	75.0		48.1		34.5		20.0		120.8	

2.2 Results of Operations for the Period January – June 2005

Sales

Sales of ICL Group in the report period amounted to approximately $1,484.0 million, compared with $1,290.6 million last year, an increase of approximately 15.0%.

The increase in the Group's sales reflects an increase in turnover in all the segments of the Group's operations, mainly as a result of price rises in many of the Company's products, as well as increased quantities sold of some of the products. The appreciation of the euro exchange rate against the dollar also contributed to some extent to the increase in income from sales in Europe, in dollar terms.

Below is a breakdown of sales by geographical markets:

Sales CIF	1-6/2005		1-6/2004		2004	
	$ millions	%	$ millions	%	$ millions	%
Israel	111.3	7.5	100.2	7.8	209.0	7.7
North America	169.7	11.4	145.1	11.2	312.6	11.5
South America	150.2	10.1	146.6	11.4	332.2	12.2
Europe	655.3	44.2	619.6	48.0	1,186.5	43.7
Asia	337.8	22.8	225.0	17.4	549.9	20.3
Rest of the world	59.7	4.0	54.1	4.2	124.8	4.6
Total	1,484.0	100.0	1,290.6	100.0	2,715.0	100.0

The breakdown of sales in the first half of the year shows a significant increase in sales in Asia and its share of total revenue, even though income increased in all the other target markets of the Company. The increase in sales in Asia is attributable mainly to increased income from sales of industrial products and potash.

After the balance sheet date, ICL Fertilizers completed an extension agreement for supplying potash to its customers in India. Under these contracts, higher prices and the sale of larger quantities were agreed for a period of six months (until December 2005).

Gross Profit

Gross profit amounted to approximately $575.2 million, an increase of 33.1% compared with last year. The gross profit margin rose from 33.5% to 38.8% of turnover.

The increase in income as described above and the ongoing efficiency measures contributed to gross profit, despite increases in the prices of energy and some raw materials. Appreciation of the shekel and the euro against the dollar contributed to increased costs in dollar terms.

Sales and Marketing Expenses

Expenses amounted to approximately $225.9 million, an increase of about 5.6% compared with last year, mainly due to the increase in the Company's sales .

General and Administrative Expenses

These expenses totaled approximately $52.1 million, compared with $52.3 million last year. Despite the effect of the appreciation of the euro and shekel exchange rates on the expenses, the Company's efficiency and savings measures kept overhead expenses stable in dollar terms.

Research and Development Expenses

R&D expenses (net of grants from the Chief Scientist) amounted to approximately $15.5 million, an increase of about $0.7 million compared with last year.

Operating income

Operating income increased by some 86.1% compared with last year, reaching $281.7 million. The percentage of operating income out of sales is 19.0%, compared with 11.7% last year. This was due mainly to price rises in most areas of the Group's operations and to the efficiency measures mentioned above.

Financing Expenses

Financing expenses amounted to about $1.2 million, compared with $18.6 million last year.

During the report period, the Company recorded income of approximately $14.0 million from exchange rate differentials. In addition, financing income / expenses were influenced by a decrease of approximately $421 million in the average balance of net financial liabilities in the half, compared with the corresponding half last year, which was partially offset by the rise in the average dollar interest rates for the period by approximately 1.3%.

Income Tax

The income tax expense in the report period amounted to $86.8 million, which is approximately 31% of pre-tax income, compared with 21% last year.

In June 2004 the Knesset enacted an amendment to the Income Tax Law, prescribing a gradual lowering of the corporate tax rate from 36% to 30%. As a result of this amendment, the income tax expense (current and deferred) charged to the statement of operations in the second quarter of 2004 decreased by approximately $18 million.

With regard to reduction of the tax rate after the date of the financial statements, see Section 9.3.

Net Income

Net income amounted to $196.5 million, compared with $106.9 million last year, an increase of 83.8%.

2.3 Results of operations for the period April – June 2005

Sales

Sales of ICL Group in the quarter amounted to $773.9 million, compared with $671.5 million last year, an increase of approximately 15.3%.

The increase in sales reflects an increase in operation turnovers of all the segments of operation of the Group, particularly in the Fertilizers segment, mainly as a result of price rises. The appreciation of the euro against the dollar also contributed to the increase in income from sales in Europe.

The table below shows the geographical breakdown of sales in the second quarter of 2005:

	4-6/2005		4-6/2004	
	$ millions	%	$ millions	%
Israel	58.0	7.5	52.7	7.9
North America	85.5	11.0	78.8	11.7
South America	126.3	16.3	101.4	15.1
Europe	321.7	41.6	287.7	42.9
Asia	152.4	19.7	128.6	19.1
Rest of the world	30.0	3.9	22.3	3.3
Total	773.9	100.0	671.5	100.0

The breakdown of sales in the quarter indicates an increase in the proportional part of sales in South America (mainly fertilizers to Brazil) and in Asia, where income increased mainly due to price rises.

Gross Profit

Gross profit amounted to $296.1 million, an increase of 27.7% compared with last year. The gross profit margin increased from 34.5% to 38.3% of total turnover.

The increase in income and the ongoing efficiency measures contributed to gross profit despite the rise in the prices of energy and some raw materials. The appreciation of the shekel and the euro against the dollar contributed to an increase in costs in dollar terms.

Sales and Marketing Expenses

These expenses amounted to $120.0 million, an increase of about 11.8% compared with last year, which was due mainly to the increase in the Company's sales.

General and Administration Expenses

These expense amounted to $26.4 million, a slight decrease compared with $27.2 million last year, despite the appreciation of the shekel and the euro against the dollar, which increased the dollar value of expense items. Continuous efforts to streamline expenses contributed to the reduction of fixed costs.

Research and Development Expenses

R&D expenses (net of grants) amounted to $7.5 million, an increase of about $0.5 million compared with last year.

Despite the effects of appreciation of the euro and the shekel on these expenses, savings and efficiency measures were able to keep overhead expenses stable in dollar terms.

Operating Income

Operating income increased by 57.5% compared with last year, and reached $142.2 million. Operating income out of sales amounted to 18.4% compared with 13.5% last year, mainly as a result of if the price rises in most areas of ICL Group's operations and the aforementioned savings and efficiency measures.

Financing Expenses

Financing income amounted to $3.5 million, compared with expenses of $10.0 million last year.

During the report period, the Company recorded income of approximately $10.0 million from exchange rate differentials. In addition, financing income / expenses were influenced by a decrease of approximately $430 million in the average balance of net financial liabilities in the second quarter, compared with the corresponding quarter last year, which was partially offset by the rise in the average dollar interest rates for the period by approximately 1.3%.

Income Tax

The income tax expense in the second quarter amounted to $44.2 million, which is approximately 30% of pre-tax income, compared with about 8% last year.

In June 2004 the Knesset enacted an amendment to the Income Tax Law, prescribing a gradual lowering of the corporate tax rate from 36% to 30%. As a result of the amendment, the tax expense on income (current and deferred) charged to operations in the second quarter of 2004 decreased by approximately $18 million.

With regard to reduction of the tax rate after the date of the financial statements, see Section 9.3.

Net income

Net income amounted to approximately $101.2 million, compared with net income of $74.6 million in the second quarter of 2004, and increase of about 35.6%.

3. Segments of Operation

The segments of operation of ICL are presented below according to the managerial division described in Section 1.1 above.

Sales CIF	1-6/2005		1-6/2005		4-6/2005		4-6/2004	
by segment	$ millions	% of total sales	$ millions	% of total sales	$ millions	% of total sales	$ millions	% of total sales
ICL Fertilizers	809.5	50.4	697.0	50.2	428.2	51.2	363.0	50.1
ICL Industrial Products*	380.9	23.7	322.8	23.3	197.2	23.6	173.2	23.9
ICL Performance Products	316.3	19.7	283.8	20.5	162.9	19.5	144.7	20.0
ICL Metallurgy	57.9	3.6	43.6	3.1	27.2	3.3	22.4	3.1
Others and setoffs	(80.6)		(56.6)		(41.5)		(31.8)	
Total	1,484.0		1,290.6		773.9		671.5	

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

Operating income	1-6/2005		1-6/2004		4-6/2005		4-6/2004	
by segment	$ millions	% of total sales	$ millions	% of total sales	$ millions	% of total sales	$ millions	% of total sales
ICL Fertilizers	168.9	20.9	104.4	15.0	85.8	20.0	58.8	16.2
ICL Industrial Products*	68.9	18.1	22.6	7.0	34.3	17.4	14.4	8.3
ICL Performance Products	36.1	11.4	24.8	8.7	18.4	11.3	17.0	11.7
ICL Metallurgy	1.4	2.5	(3.2)	(7.4)	0.2	0.8	(1.5)	(6.5)
Others and setoffs	6.4		2.8		3.5		1.6	
Total	281.7	19.0	151.4	11.7	142.2	18.4	90.3	13.5

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

3.1 ICL Fertilizers

Sales

The volume of operations in the segment amounted to $809.5 million, an increase of 16.1% compared with last year. The increase in sales turnover arises mainly from high prices for most of the segment's products as a result of ongoing price rises in the world's fertilizer markets. The appreciation of the euro and the pound sterling against the dollar also contributed to the rise in prices in dollar terms.

Operating income

Operating income in the segment amounted to $168.9 million, an increase of 61.7% compared with last year. The operating margin on sales was 20.9%, compared with 15.0% last year. The improved operating income was achieved mainly as a result of the increase in income noted above. However, an increase in various production costs, principally energy costs, and the effect of the appreciation of the shekel on the shekel expenses of the segment in dollar terms, moderated the positive effect on operating income. Marine transportation prices decreased significantly compared with the record

high in December 2004, and although still relatively high, the downward trend is continuing.

During the second quarter last year, Negev Minerals was sold and the results of its operations are no longer included in the segment's expenses.

Potash

Sales revenue from potash includes the sales from Sdom, Spain and England..

Potash – Sales Revenue and Income

Thousands of dollars	1-6/2005	1-6/2004	4-6/2005	4-6/2004	2004
Income*	547.1	440.5	279.0	233.9	923.3
Operating income	154.1	104.9	77.5	58.5	231.0

* Including sales revenue from inter-segment sales

The increase in sales revenue is the result of the ongoing rise in the prices of potash together with a slight decrease in quantities sold. The improvement in operating income, which increased in the report period by 46.9%, derives primarily from the improvement in the selling prices.

Potash – Production and Sales

Thousands of tons	1-6/2005	1-6/2004	4-6/2005	4-6/2004	2004
Production	2,636	2,587	1,330	1,276	5,387
Sales to external customers	2,475	2,615	1,244	1,465	5,137
Sales to internal customers	139	141	73	75	280
Total sales (including internal sales)	2,614	2,756	1,317	1,540	5,417

Production in the period and in the quarter was 50,000 tons higher than in the corresponding period last year. Sales to external customers and for internal uses (mainly for the production of compound fertilizers) were approximately equal to production, whereas last year, part of the quantities of potash sold was accumulated stocks from prior periods.

Brine percolation exists at one of the dikes of the evaporation ponds of the ICL Fertilizers segment at the Dead Sea. After 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, compound and specialty fertilizers), fertilizer-grade (green") phosphoric acid used as a raw material for the production and downstream products, as well as other products.

Fertilizers and Phosphates – Sales Revenue and Income

Millions of dollars	1-6/2005	1-6/2004	4-6/20054	4-6/2004	2004
Income*	280.7	267.7	158.7	132.2	550.4
Operating income	14.4	(0.6)	8.2	0.9	12.9

* Including sales revenue from inter-segment sales.

The increase in sales revenue compared with the same period last year derives mainly from price rises and from larger quantities of phosphate fertilizers sold in Europe in the second quarter, which offset the smaller quantities of fertilizers sold in the first quarter.

The increase in operating income in the period compared with the first half of last year stemmed from the price rises and from the disruption in production in the first quarter of last year. The improved operating income was achieved in spite of the rise in the prices of energy and other inputs, and the appreciation of the shekel against the dollar.

Fertilizers and Phosphates – Production and Sales

Thousands of tons	1-6/2005	1-6/2004	4-6/20054	4-6/2004	2004
Phosphate rock					
Production	1,713	1,573	826	843	3,290
Sales*	187	288	106	153	566
Fertilizers					
Production	830	825	413	440	1,696
Sales*	806	854	483	396	1,664

* 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 volume of sales of rock in the period derives 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.

During the report period, ICL Fertilizers continued the construction of a plant at its site in Mishor Rotem, for the production of technical grade mono-ammonium phosphate (MAP), mainly for use as a soluble fertilizer.

3.2 ICL Industrial Products

Sales

Sales in this segment in the report period amounted to $380.9 million, an increase of about 18.0% compared with last year. The increase in sales derives mainly from a sharp rise in prices in almost all the areas of the segment's operations and an increase in the quantities sold of some products.

Sales revenue from flame retardants increased considerably, mainly as a result of price rises in most of the products and despite the slowdown in the printed circuits market, which led to slower sales.

Sales revenue from inorganic bromine products increased, particularly elementary bromine and clear brines, due to increased demand, and in the oil and gas industries, which led to price rises.

Sales of agricultural products decreased in quantities sold in the period compared with last year, due in part to smaller quotas for use of methyl bromide for soil fumigation in Europe and developing countries, and in part due to sales of methyl bromide brought forward to the first half of last year. Nevertheless, operating income was not adversely affected.

In biocides for water treatment, sales revenue increased as a result of price rises following a levy against dumping which was imposed on chlorinated biocides imported to the U.S.A. from China and Spain.

In magnesia products for the refractory industry and other uses, sales revenue increased following price rises, which was partially offset by smaller quantities sold.

Sales revenue from chlorine-based products from the Dead Sea (Dead Sea salts) increased, due in part to price rises..

Montreal Protocol

Under the accord known as the "Montreal Protocol", to which Israel is a signatory (and which was adopted as part of Israel's local legislation), the manufacture and consumption of methyl bromide for soil fumigation in developed countries will gradually be reduced to zero by the year 2005, except for "critical uses" approved by the parties to the accord from time to time. The quantities approved for production and sale in 2005 are similar to those approved for 2003 and 2004 except in western Europe, where the member countries decided voluntarily to reduce quantities to about 65% compared with 2004.

According to UNEP (United Nations Environment Programme) publications, it was agreed that in 2006, quantities of production and sales for critical uses in developed countries will be cut by about 20% compared with quantities approved in 2005 , but the final decision has not yet been made.

Sales in the first half of 2005 of agricultural products that might be banned accordingly in 2006, amounted to approximately $11 million, with an operating income in respect of those sales of about $4 million.

Commencing January 1, 2005, the quantity of methyl bromide that can be sold to developing countries for soil fumigation was cut by a one-time reduction of 20%. This quota will remain in effect until 2015, after which the quantity will be reduced to zero, subject to critical uses as approved by the parties to the treaty from time to time.

Methyl bromide has other uses apart from soil fumigation, for which production and consumption quantities are unlimited, such as pre-shipment and quarantine treatment, as a raw material or intermediate material for the manufacture of another material or product (feedstock). These uses are not within the purview of the Montreal Protocol.

ICL Industrial Products intends to remain in the soil fumigation field even after the ban on use of methyl bromide as aforesaid. Accordingly, in recent years it has been investing efforts in the development and marketing of substitute and complementary products for methyl bromide in this important market.

Total sales of agricultural products in the first half of 2005 for uses which are not restricted under the Montreal Protocol and to developing countries, were about $21 million, with an operating income in respect of those sales amounting to approximately $8 million.

Operating income

Operating income in the segment was approximately $68.9 million, an increase of about 204.6% compared with last year.

The increase stemmed mainly from increased sales revenue and from the continued improvement in the efficiency of the segment's operations. The increase in operating income was offset by a rise in the costs of production and overhead. Particularly noteworthy is the rise in the prices of some of the raw materials, and costs of energy and marine transportation.

3.3 ICL Performance Products

Sales

Sales in this segment amounted to approximately $316.3 million, an increase of about 11.4% compared with last year. The increase in sales turnover derives from a rise in selling prices and the effects of appreciation of the euro against the dollar, and from increased quantities sold of some of the segment's product lines, notably food

additives. Conversely, the ongoing economic slowdown in Europe, the surplus production capacity in some of the markets for the segment's products and intensifying competition with companies whose expenses are denominated in dollars, adversely affected the sales of the segment in some of its areas of operations.

Operating income

Operating income in the segment amounted to $36.1 million, about 45.6% higher than in the same period last year. The margin was about 11.4%, compared with 8.7% last year.

This increase in sales revenue, along with operational improvements in some of the segment's operations, particularly white acid (food-grade phosphoric acid), contributed to the improvement in profitability. Conversely, increased costs of important production inputs, especially the rise in the prices of raw materials and energy, partially offset the improvement. The appreciation in the euro-dollar exchange rate also had an adverse effect on profitability from sales of products to customers whose purchases are denominated in dollars.

3.4 ICL Metallurgy

Sales

Sales in this segment amounted to $57.9 million, an increase of about 32.8% compared with last year.

The increase in sales derives mainly from a rise in selling prices of the various types of magnesium, due partly to the strengthening euro against the dollar and to increased quantities sold, along with a rise in the share of magnesium alloys in the sales mix. The levy imposed in the U.S.A. following a ruling by the authorities there that magnesium manufacturers from China and Russia sold at dumping prices, is the principal factor that led to a rise in the prices of magnesium in the American market in the report period.

Operating income

Operating income in the segment amounted to $1.4 million, compared with an operating loss of about $3.2 million in the same period last year. The improved income is due mainly to the price rises noted above, which were offset by a rise in the prices of some production inputs, particularly energy and materials expenses.

4. The financial position of the Group

ICL's policy is to reduce its financial leverage while diversifying sources of financing among various financial instruments and between local and foreign sources.

In the report period, the trend of decreasing net financial liabilities of the Group continued, and at the end of the period those liabilities amounted to $450.0 million after a decrease of $119.0 million during the period that was achieved by directing free cash flow to this purpose.

The Group's sources of financing are primarily short-term and long-term loans from Israeli and international banks. On March 4, 2005 ICL Group closed a transaction with foreign institutional investors in which it raised $125 million for a period of five to ten years (average repayment period – 8 years), at interest varying between LIBOR + 1% and LIBOR + 1.15%.

After the balance sheet date, a syndicated loan transaction was signed with 16 international banks, for $250 million ($100 million loan and $150 million credit facility) for a period of 5 years (bullet) at LIBOR + 0 6% interest.

Cash flows

ICL's cash flow from current operations in the first half of 2005 amounted to approximately $243.1 million, compared with $205.5 million in the same period last year, an increase of about $37.6 million. These amounts were the principal source for financing investments in property, plant and equipment of $75.0 million and for decreasing the Group's net financial liabilities.

5. Investments

In the report period, investments in property, plant and equipment net of investment grants amounted to approximately $75.0 million, compared with investments in property, plant and equipment less grants amounting to $48.1 million in the same period last year.

6. Human Resources

The total number of employees at ICL Group as at June 30, 2005 is 8,557, compared with 8,546 on December 31, 2004. The increase is mainly in the ICL Industrial Products segment, due to increased activity in China.

Under a collective agreement signed in 1978 with the employees of the subsidiary Dead Sea Works ("DSW") of the ICL Fertilizers segment, an arrangement was made which regulates the early retirement of workers at the Sdom plant. Following the decision of the National Labor Court declaring that arrangement void, DSW negotiated with the Workers' Committee, as a result of which a collective agreement was signed on July 19, 2005, granting DSW workers in the Sdom plant to whom it applies, a right to early retirement from the age of 60, provided certain conditions are met.

7. Exposure to Market Risks and their Management

No material change occurred during the report period, compared with the Directors' Report for 2004.

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

No material change occurred during the report period, compared with the Directors' Report for 2004.

9. Events during the period

9.1 Commencing May 1, 2005, Mr. Shmuel Ben-Shimol, CPA, a partner in the firm of Deloitte – Breitman Almagor and internal auditor at several companies, was appointed as internal auditor of the Company. The previous internal auditor has transferred to another position within the ICL group.

9.2 On April 20, 2005 the Company distributed a dividend of approximately $35.7 million. On August 22, 2005 the Company decided to distribute a dividend of approximately $ 60 million on September 21, 2005.

9.3 On July 25, 2005 the Knesset passed the second and third readings of a bill for Amendment of the Income Tax Ordinance (No. 147 and temporary order), 5765-2005 ("the 2005 Amendment"). The 2005 Amendment revises for the second time the corporate tax rates prescribed in the 2004 Amendment, and determines that the corporate tax rate will be reduced gradually, commencing January 1, 2006 in the following manner: 2006 – 31%, 2007 – 29%, 2008 – 27%, 2009 – 26% and from 2010 onwards – 25%.

As a result of the 2005 Amendment, the income tax expenses of the Company can be expected to be reduced by approximately $26 million (based on the deferred tax

balances as at June 30, 2005), which will appear in the statement of operations of the third quarter of 2005.

9.4 On August 22, 2005 the Board of Directors of the Company approved an investment of approximately $36 million for expanding the production in the raw material array of the carnallite pools in Sdom by about 250,000 tons.

9.5 In July 2005 ICL Performance Products acquired the Brazilian company Adicon, which manufactures and supplies additives for the food industry in Brazil.

9.6 On August 4, 2005 a desalination facility started operation in Ashkelon. The plant was erected by V.I.D. company. under a B.O.T. agreement with the State of Israel for the construction and operations of a desalination plant which will supply 100 million cubic meters of potable water per year over a period of 25 years.

V.I.D.. is owned by IDE Technologies (50%) and other partners. IDE is under the joint control of ICL and the Delek Group.

9.7 On July 28, 2005 the Securities Authority published a directive according to Section 36A(b) of the Securities Law, 5728-1968, requiring disclosure concerning grant of consent to a "peer survey", the purpose of which, according to the directive, is to initiate a control process for the work of auditing firms and to ascertain the fulfillment of the procedures required during their auditing work, which will improve the performance of the capital market. The Company and its Board of Directors see a survey of this kind in a positive light, and accordingly, the Company is ready to cooperate in promoting the process. Nevertheless, consent to participate in the survey, in the format required today, involves serious legal questions relating, inter alia, to protection of the confidentiality of the information that the Company makes available to the auditors, prevention of conflicts of interests, and the liability of the surveyors towards the Company in the event of their failure to maintain confidentiality. As at the date of publication of this report, no satisfactory solution has been found for these questions in the survey documents submitted to the Company. The Board of Directors therefore resolved to withhold, at this stage, the consent requested of the Company for the "peer survey", until such a solution is found.

The matter was not discussed by the General Assembly of the Company which appointed its auditors for 2005, as that meeting took place before the publication of the directive.

The Company is satisfied with the propriety of the auditing of its financial statements by its auditors, *inter alia* in that it has chosen one of the four large international firms as its auditors, all of which have defined work procedures.

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.

August 22, 2005

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