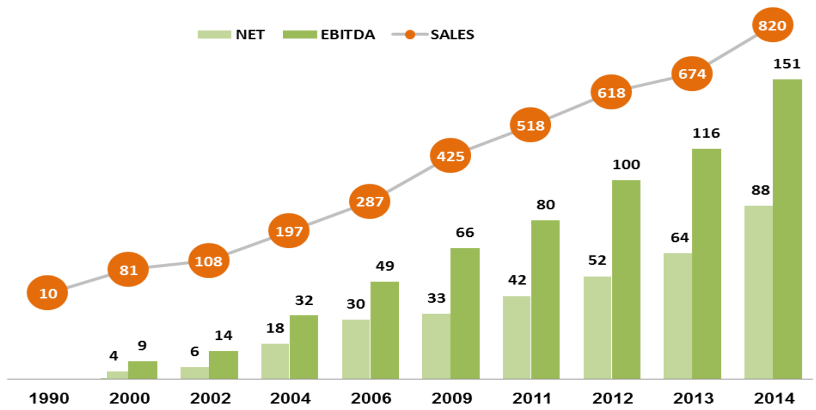
Frutarom Industries Ltd.

Annual Report 2014

Dear Shareholder,

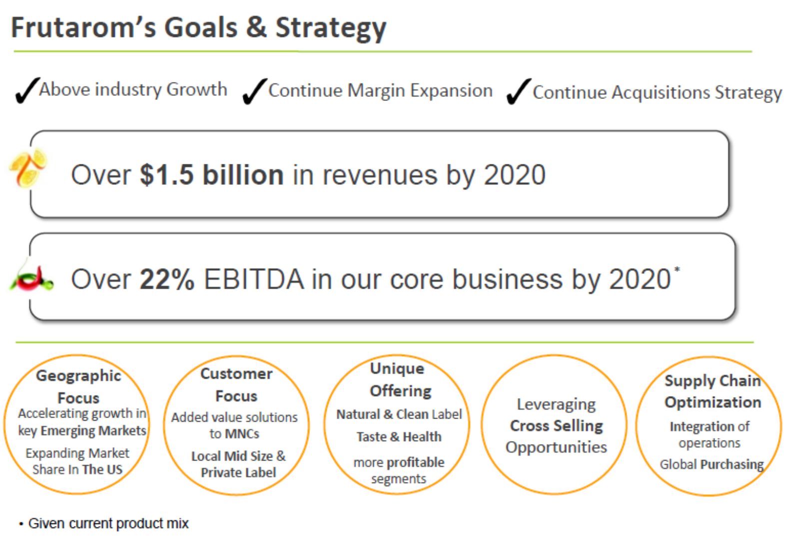
We are pleased to sum up another record year for Frutarom - a year in which we achieved another quantum leap in our journey of rapid and profitable growth, and in positioning ourselves as a leading global player in the fields of Flavors and Specialty Fine Ingredients. The continued successful implementation of our strategy combining profitable organic growth with strategic acquisitions has led to our growing at an average annual rate of 18% since 2000, supported by rapid organic growth and the execution of 41 acquisitions. Over this period, our Flavors activity has grown at an average rate of 25% a year and Frutarom revenues and profits have increased ten-fold, from $81 million of revenues and an EBITDA of $9 million to record high revenues of $820 million and EBITDA of $151 million, with net income reaching $88 million and having more than doubled since 2011.



The improvement in profits and profit margins of our core businesses, which include the Flavors and Specialty Fine Ingredients activities, has continued and the ambitious goal we set for ourselves of reaching EBITDA of 20% by 2016 has already been reached this year.

We are confident in our ability to continue fulfilling our ambitious strategic plans and strengthening our position in the world, to attain a higher growth rate than the rate of growth in the markets in which we operate, and to continue improving our profits and profit margins.

Our strategic plan for the next five years will lead to achieving the goal of at least $1.5 billion in sales with an EBITDA margin of over 22% in our core businesses by 2020.



Our strategic plan includes continuing to focus on five main areas:

1. Continued improvement in our **geographic sales mix** while substantially increasing sales in the United States and the expanding emerging markets (with emphasis on Southeast Asia, Latin America and Africa);

2. Continued improvement of **our product mix** along with continued rapid and more profitable growth for both our Flavors activity and our Specialty Fine Ingredients activity, with emphasis on unique and innovative natural products that match future global consumer preferences;

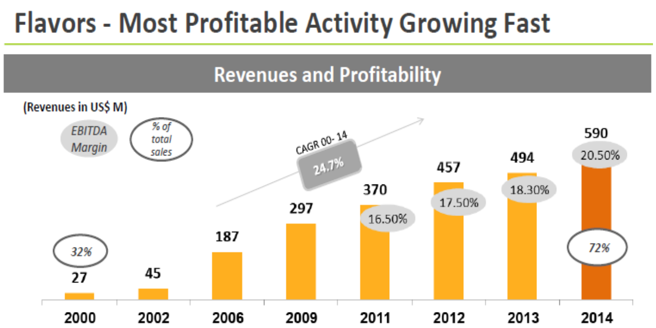
3. Developing and providing unique solutions to our **large multinational customers**, and providing a portfolio of comprehensive solutions in the fields of taste and health to **medium-sized and local customers**;

4. Reaping maximum benefit from the many **cross-selling opportunities** among our diverse operations, to which the acquisitions we performed and will perform also contribute;

5. Continued **improvement in our profit margins and profits** through optimal use of our resources, from acquisitions too, and through the generating of operational savings, the building of a global procurement system, and reinforcement of our competitive capabilities.

Meeting our ambitious targets has led to record results:

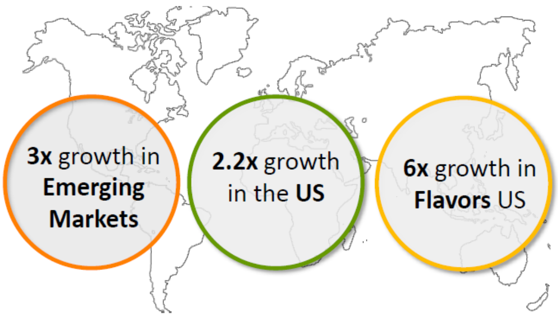
The implementation of our strategy to **significantly increase the share of our Flavors activity,** the most profitable of our activities, has led to the Flavors activity reaching a 73% share of overall Frutarom sales (compared with 33% in 2000) while achieving a growth rate that is higher than that of the markets in which we operate, along with continued improvement in profits and margins.

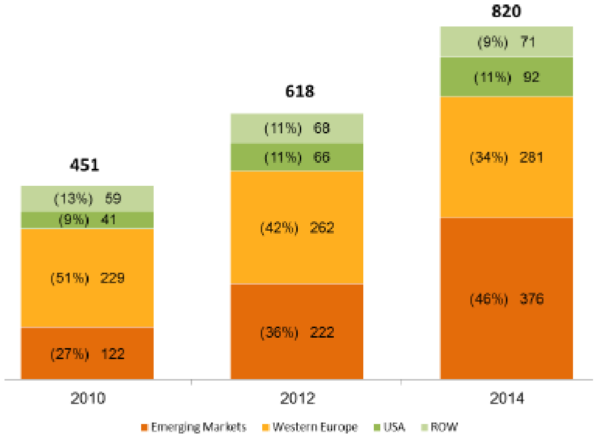


Over the last few years we have worked to **improve the product mix in the Specialty Fine Ingredients activity** as well. Our R&D labs have successfully developed new and innovative natural specialty ingredients targeted for both the taste and the health markets. Successful penetration of these products has contributed – and will continue to contribute – to an increase in sales for our Specialty Fine Ingredients activity as well as an improvement in margins. Under this strategy we are expanding the portfolio of natural products we offer our customers. Over the last few months we entered the growing field of natural colors (through the acquisition of Montana Food, Vitiva, and Ingrenat) and significantly expanded our activity in the growing field of natural antioxidants that promote food protection.

Frutarom's rapid expansion into fast-growing emerging markets was implemented with the support of profitable internal growth and strategic acquisitions:

<u>Distribution of sales by geographic area 2010-2014:</u>

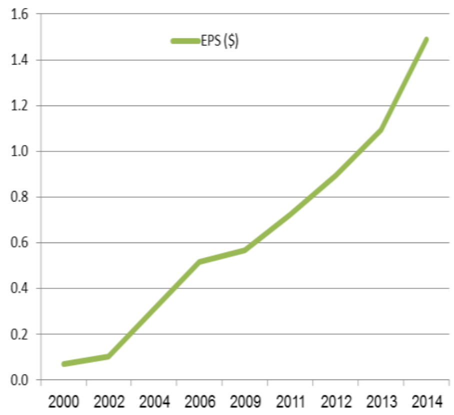




Over the last four years we have tripled our sales in emerging markets and their share in overall sales has risen from 27% in 2010 to 46% this year. At the same time we have doubled sales in the United States, the world's largest market for flavor extracts, while Flavors activity in North America, on which we focused, grew six-fold. The six acquisitions we executed in 2013 and 2014 (**JannDeRee** in South Africa, **PTI** in Russia, **Aroma** in Guatemala, **Hagelin** in the US which also has sales to Africa and Latin America, **CitraSource** in the US, and **Montana Food** in Peru and Chile) are also contributing and will keep contributing towards accelerating growth and increasing Frutarom's sales and market share in emerging markets and the United States. We have also worked and will continue to work on focused reinforcement of our R&D, production, and sales and marketing platforms in important target countries. So it is that in the past four years we have built a growing Flavors activity in Central and South America and in Africa, we have established a market leadership position in the markets of Eastern and Central Europe, we expanded our sales platform in India where we have set up a new Flavors operation, and we have added sales and marketing resources in Southeast Asia - in Indonesia, the Philippines, Thailand, Vietnam and Sri Lanka, as well as in China where our new factory is in the final stages of construction.

2014 – 2015 acquisitions:

Frutarom's rapid sales growth in recent years has also translated into a significant increase in profits, profit margins and the strong cash flow that we achieve:
In 2014 the gross margin for core activities (Flavors and Specialty Fine Ingredients) reached 41.0%. Operating profits for core activities rose 35.8% and reached a record level $116.2 million with an operating margin of 15.7%. EBITDA rose 28.7% to a record $148 million on a margin of 20%.
Net income and earnings per share climbed 37.7% and 36.7% respectively to reach $87.6 million and $1.49 per share compared with $63.6 million and $1.09 per share in 2013. Net margin reached 10.7% compared with 9.4% in 2013.



Contributing to the considerable improvement in core business profits and profitability are organic sales growth, improvement in the product mix, and measures we are taking to achieve maximum operational efficiency. We will continue to work toward optimizing our resources, generating substantial operational savings and strengthening our competitive capabilities. We are also continuing to build up our global procurement system and exploit the significant purchasing power that Frutarom has gained through the growth of its activity and its recent acquisitions, while expanding our circle of suppliers and emphasizing the purchase of raw materials used in the production of our products, and natural raw materials in particular, directly from their countries of origin.

We have continued to establish and strengthen our position as one of the world's ten largest and leading flavors and specialty fine ingredients companies, uniquely positioned at the crossroad between the growing fields of taste and health. The rapid transition by food and beverage companies towards the use of natural raw materials and flavors in the wake of consumer demand has continued, with an emphasis on low-fat, low-sodium, and low-cholesterol foods bearing the Clean Label which are perceived as more nutritious, healthier and more environmentally friendly. Frutarom, with about 2/3 of its products being natural, has uniquely positioned itself as a provider of unique and innovative solutions using advanced technology in combining flavor and health, towards fulfilling its vision:

"To be the Preferred Partner for Tasty and Healthy Success"

We will continue expanding our market share among large multinational customers to whom we offer unique innovative products, as well as with medium-sized and locally-based customers, with an emphasis on providing them service customized to their unique needs, including technological and marketing support, assistance in the development of products, and top quality service along with tailor-made solutions as usually provided to large multinational companies. Special focus is being placed on increasing our market share among private label customers (a sector growing faster than the branded food industry) that already make up 1/3 of our Flavors activity sales.

Frutarom today is one of the leading global players in the industry, with an extensive range of products, wide geographic spread and a diversity of superb customers. We have succeeded in achieving the ambitious goals we set for ourselves and have made a quantum leap in our activities. The continued successful implementation of our strategy, deeper penetration into the high-growth emerging markets and the United States, the steps we are taking to consolidate and optimize our operational resources and procurement, and the successful integration of our acquisitions, along with our excellent pipeline of future acquisitions and robust financial structure, will lead to a another quantum leap in revenues, profit and margins for Frutarom. We believe in our ability to continue accomplishing our strategic plan and our ambitious targets and to reach sales turnover of at least $1.5 billion along with an EBITDA margin of over 22% from our core business (Flavors and Specialty Fine Ingredients) by 2020, and continue to driving up value for our shareholders.

We are certain that with the cooperation of our employees led by our global management team and with the ongoing support of the members of the Board of Directors and from you, our shareholders, we will be able to continue expanding and successfully meet the ambitious goals and challenges ahead.

Sincerely Yours,

Dr. John Farber	Ori Yehudai
Chairman of the Board of Directors	President & CEO

March 16, 2015

TABLE OF CONTENTS

FORWARD-LOOKING STATEMENTS

This report includes forward-looking statements. Forward looking statements, as the term is defined in the Securities Law – 1968, include data, forecasts, evaluations, estimations or other information relating to future events or circumstances the occurrence of which is not certain and which are not solely in the Group's control. Forward-looking statements can be identified, among other things, by the fact that they include terms such as "it is the Group's estimate" or "the Group's management estimates", "the Group intends", "the Group believes" and other similar expressions. Forward looking statements include, among other things, discussions on strategy, plans, objectives, goals, projections, future events and intentions, including revenue, profit and profitability targets and plans relating to acquisitions the Company has made, and to the integration and utilization of business and operational synergies resulting from such.

By their nature, forward-looking statements are subject to uncertainties and risks. The actual results of the Group's activity, its financial state and development, including the realization of its strategy and goals, could be materially different to those described or discussed in this report.

The forward-looking statements appearing in this report are based on estimations made by the Group's management which are based, among other things, on the information available to the Group's management at the time of publication, including estimation regarding Frutarom's area of activities, goals, objectives, strategy, and future events and intentions.

The main factors which could cause the results of the Group's activities, financial status and development, including realization of its strategy and goals, to materially differ from those described in this report include, among other things, effects of the global economy; competition in markets in which the Group operates; changes in demand for the Group's products; the Group's failure to successfully identify or carry out future acquisitions of companies or activities; the impact of laws, regulations and standards, especially in the areas of environmental protection; health and safety; changes in currency exchange rates; and fluctuations in the prices of raw materials used by the Group and its ability to acquire these.

SECTION A

DESCRIPTION OF THE COMPANY'S BUSINESS

TABLE OF CONTENTS

The following terms will have the meaning ascribed to them:

“Aroma”	The Guatemalan Aroma Group
“CitraSource”	The business activity and assets of CitraSource LLC and 100% of the issued share capital of CitraSource LLC Holdings of Florida, USA
“Directors' Report”	Report of the Board of Directors of the Company as at Dec. 31, 2014, attached as Chapter 2 to this report.
"EAFI"	East Anglian Food Ingredients Ltd.
"Etol"	FRUTAROM ETOL Tovarna arom in eteričnih olj d.o.
"Financial Statements"	The financial statements of the company as of December 31, 2014, attached as Chapter 3 to this report
"GDRs"	Global Depositary Receipts
"Hagelin"	Hagelin & Company Inc. and BRC Operating Company LLC
"Ingrenat"	Ingredientes Naturales Seleccionados, S.L
"JannDeRee"	JannDeRee(Pty)
"Montana Food"	The flavors and natural colors for food division of the Peruvian company Montana S.A.
"Mylner"	Mylner Indústria E Comércio Ltda and its parent company, Vila Osório Participações s/a
“PTI”	The Russian Protein Technologies Ingredients Group
"Savoury Flavours"	Savoury Flavours (Holding) Limited and its subsidiaries
"Share"	Ordinary share par value NIS 1.00 of the Company - Frutarom Industries Ltd.
The "Company"	Frutarom Industries Limited
The "Group" or "Frutarom"	Frutarom Industries Limited, including its consolidated companies
The "Companies Law"	The Companies Law, 1999

The "Ordinance"	Income Tax Ordinance (New Version)
The "Securities Law"	The Securities Law, 1968
"US$"	United States dollar(s)
"Vitiva"	VITIVA proizvodnja in storitve d.d of Slovenia

All financial data in this report is in US dollars unless stated otherwise.

CHAPTER 1 – THE COMPANY'S BUSINESS AND ITS DEVELOPMENT

1. ***The Group's Activity and Description of its Business Development***

General

1.1. Frutarom was incorporated in Israel in 1995 as a private limited stock company under the name Frutarom NewCo (1995) Ltd. In 1996 the Company's shares were listed for trading on the Tel Aviv Stock Exchange, and the name of the Company was changed to Frutarom Industries Ltd.

1.2. Frutarom Ltd., a wholly owned subsidiary of the Company through which the Company's business and production activities are held, was established in 1933 as Frutarom Palestine Ltd. Frutarom's operations initially consisted of the cultivation of aromatic plants and flowers for the extraction and distillation of flavor and fragrance substances and essential oils.

1.3. In February 2005 the Company raised capital from investment institutions in Israel and abroad by issuing shares and registering GDRs for trading on the London Stock Exchange Official List.

1.4. Frutarom is now a global company, one of the world's ten top companies in the field of flavors and specialty fine ingredients. Frutarom develops, produces and markets comprehensive solutions in the field of flavors and specialty fine ingredients used for the production of food, beverages, flavor and fragrance extracts, pharmaceutical/nutraceutical products, cosmetics and personal care products, and other products. Frutarom operates 37 production sites, 42 research and development labs, and 73 sales and marketing centers in Europe, North America, Latin America, Israel, Asia and Africa, marketing and selling more than 31,000 products to over 16,000 customers in more than 150 countries and employs roughly 3,100 people throughout the world.

1.5. Frutarom has adopted a strategy which combines rapid and profitable internal growth with acquisitions and leveraging of synergies which these bring about.

In the framework of this strategy, Frutarom has focused In recent years on the following objectives:

- **Expanding its global reach**. Frutarom is focused on maintaining and stepping up its growth and broadening its market share. The Company strives to make inroads in high-growth **emerging markets** such as in China, South and East Asia, and Central and South America, as well in Central and Eastern Europe, Africa, and **the United States**, with the objective of capitalizing on the higher growth potential and the abundance of business opportunities to be found in these markets.

- **Developing new products and solutions that combine taste and health.** Frutarom develops innovative taste and health solutions addressing customers' requirements and future needs. These solutions are in line with the major trends in the global food market and with consumer demand, including the combination of taste and health, health supplements, anti-aging products and food products targeting specific population and age groups. The added value offered by Frutarom and Frutarom's unique abilities to combine taste and health solutions give the Company an important competitive advantage among customers in both developed and emerging markets. These innovative products carry for the most part higher margins, thereby contributing not only to sales growth but also to an improved product mix and to Frutarom's profitability.

- **Focusing on natural products**. Frutarom is working on developing and expanding its portfolio of natural products in response to consumer demand and the main trends in the global food market towards natural and healthier foods. This field is growing at a rapid pace and Frutarom's capabilities give it a competitive edge. Under this strategy, Frutarom has recently expanded its activity while also entering the field of natural food colors (by acquiring Montana Food, Vitiva, and Ingrenat) along with significantly expanding its activity in the area of natural antioxidants used in food protection solutions.

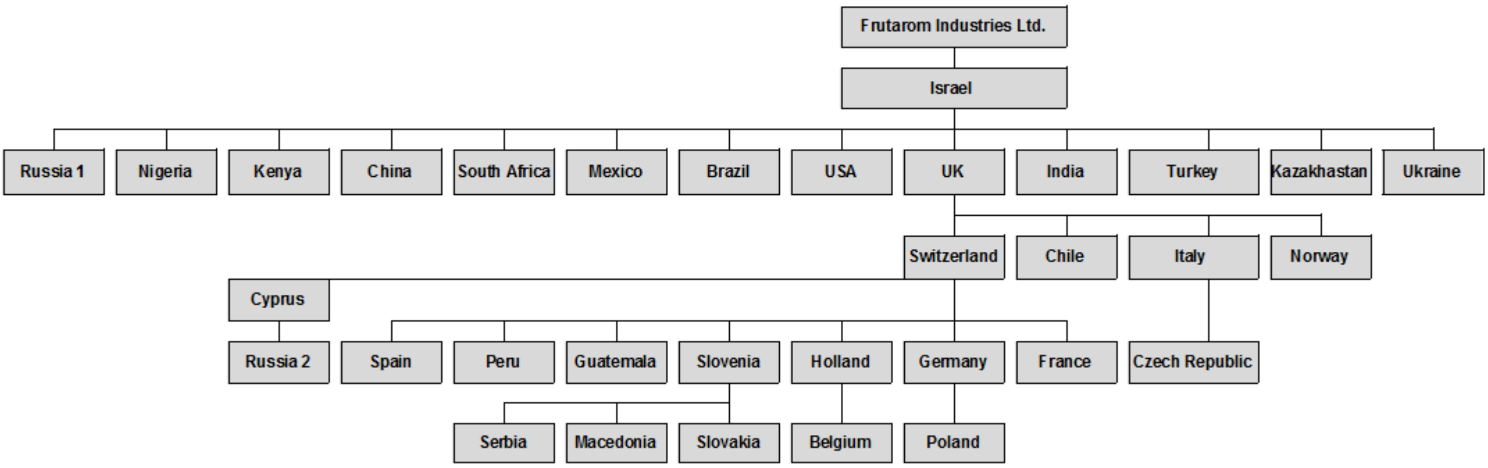
- **Focus on providing quality service and product development to large multinationals along with medium-sized and local customers.** Frutarom continues expanding its services to its customers and its product portfolio and solutions for both large multinationals and medium-sized and local companies, placing special emphasis on the fast growing private label market. In the market sector of large multinational food and beverage companies, Frutarom will continue focusing on specialty products and on expanding its natural products portfolio. For the medium-sized and local market sector which makes up a sizeable share (over 60%) of the market of food producers and also includes the private label manufacturers, Frutarom offers the same high level of service and tailor-made solutions as customarily provided to large multinational customers. Frutarom also offers its medium-sized and local customers and its private label customers, which tend to be more limited in their resources than large multinationals, assistance in developing their products by providing marketing support and flexibility on minimum order quantities and delivery dates.

- **Acquisitions and mergers and their contribution to profitable growth**. Frutarom has extensive acquisitions and mergers experience and works towards integrating its acquired companies and activities with its existing business, utilizing commercial and operational synergies in order to leverage the many cross-selling and operational savings opportunities and achieve continued improvement of its margins. Since the early 1990s, Frutarom has performed 41 strategic acquisitions, including five acquisitions in 2011, three in 2012, and four in 2013, all of which were successfully integrated with its global activities and contribute to both revenues growth and improved profitability. In 2014 Frutarom continued implementing its acquisition strategy, with a focus on expanding sales and market share in emerging markets and the United States, with the acquisitions of CitraSource in the US and Montana Food in Peru and in Chile, along with Vitiva in Slovenia, FoodBlenders in the UK, and Ingrenat in Spain at the beginning of 2015. Beyond their contribution to the profitable growth of Frutarom's existing products and activities, these acquisitions enable Frutarom to develop additional activities and create future growth engines. For example, Frutarom's latest acquisitions reflect its decision to penetrate the field of natural food colors as well as expand its activity in the area of antioxidants that help in providing natural solutions for food protection, supplementing the portfolio of products and services it offers its customers and establishing a foundation for future growth in these important areas.

For further information on the Company's growth strategy, see section 37 of this report.

1.6. The Company's main shareholder is the ICC Group[1] with holdings as of the date of this report of 21,358,034 shares, representing approximately 36.50% of the Company's share capital and voting rights.

The Group Structure as of the date of publication of this report:[2]



[1] The above is held through subsidiaries of ICC Industries Inc. In addition to these shares, 48,888 shares (approx. 0.08% of the Company's issued and paid up share capital) are directly held by Dr. John J. Farber and his wife, Mrs. Maya Farber, the principal owners of ICC Industries Inc. who also serve respectively as chairman of the Company's board of directors and director of the Company. Their daughter, Ms. Sandra Farber, also serves as a director of the Company.

[2] The structure of the Group is presented according to the main countries in which Frutarom operates (the **"Main Countries"**). Except for Frutarom subsidiaries in South Africa, Turkey, Ukraine and Cyprus, holdings in all Group companies in the Main Countries equal 100%. For further details regarding Frutarom's significant subsidiaries see Note 23 to the financial statements.

1.7. During the second half of the 1980s, upon the change of Frutarom's management, a new business strategy was adopted promoting substantial growth in the Company's international activities to turn Frutarom into a leading global company in its field by significantly expanding its Flavor operations, the Company's most profitable activity.

In the early 1990s Frutarom's management decided to expand its global activity by acquiring companies and operations within its fields of activity.

Since 2001 Frutarom has accelerated the pace of its growth by implementing a strategy combining profitable organic growth and the execution of strategic acquisitions in order to expand its business opportunities in both emerging and developed markets. Frutarom has significantly increased its mergers and acquisitions activity over these years, performing 34 acquisitions so far during this period.

1.8. Details of key acquisitions executed by the Company over the past three years are as follows:

1.8.1. **Acquisition of Savoury Flavours -** On January 4, 2012 Frutarom signed an agreement to acquire 100% of the share capital of the UK company Savoury Flavours for approx. US$ 5.8 million (£ 3.8 million) along with an additional US$ 430 thousand (£268 thousand) calculated based on performance according to a mechanism established in the agreement. The acquisition was completed upon signing.

Savoury Flavours, founded in 1999, develops, manufactures, and markets savory taste solutions, including mainly flavors, seasoning compounds, marinades and sauces, and specializing in snacks and convenience foods. Savoury Flavours has a development, manufacturing and marketing site in the UK and a wide customer base including food and private label manufacturers in the UK and emerging markets.

Sales turnover for Savoury Flavours over the 12 month period ending September 30, 2011 amounted to US$ 6.6 million (£ 4.1 million), and US$ 5 million (£ 3.2 million) during the 12 month period ending September 30, 2010 – a growth of 28%.

Savoury Flavours' production site is located near the production site acquired by the Company from EAFI, which is also involved in savory production, through an acquisition carried out in 2011. The geographic proximity between the sites and the complementary product portfolios and technologies of the two operations have allowed for the merging of their activities and placing them under shared management, creating significant synergies between the two operations and with Frutarom’s growing savory activity in the

UK and throughout the world which has increased significantly over recent years.

For further information regarding the acquisition of Savoury Flavours, see the Company's immediate report published on January 5, 2012 and Note 5(a) to the financial statements.

1.8.2. **Acquisition of Etol -** Over the first half of 2012 Frutarom purchased the entire share capital of the Slovenian company Etol for an overall sum of € 35.4 million.

Etol, founded in 1924, develops, manufactures, and markets flavor solutions for the food and beverage industry with a focus on natural flavor products.

In the nine months ending September 30, 2011 the Etol Group's sales turnover increased 7% compared with the parallel period in 2010 to reach €38.6 million (US$ 54.3 million).

Etol also has considerable experience in the development and manufacture of sweet and savory flavors, fruit-based products and food systems, specializing in local fruits of the region, as well as extensive activity in the growing area of beverage bases where Frutarom is investing and expanding its activities. Etol products are sold to a wide customer base in Central and Eastern Europe and emerging markets, with its focus on Russia, Poland, Ukraine, Slovenia, Croatia, Serbia, Slovakia, Belarus, Macedonia, Czech Republic, Kazakhstan, Turkey and other developed countries including Switzerland, Germany and the UK. Etol's customers include food and beverage manufacturers in countries in which it operates, including large multinational food companies. In 2014 Frutarom transferred some of its Israeli and Swiss flavor activities to Etol (as well as to the UK), thereby generating significant operational savings.

For further information regarding the acquisition of Etol, see the Company's immediate reports published on January 17, 18 and 26, 2012, February 12, 2012, March 17, 2012, May 8, 2012, and June 6 and 26, 2012 and Note 5(b) to the financial statements.

1.8.3. **Acquisition of Mylner -** on February 7, 2012 Frutarom signed an agreement, to acquire 100% of the share capital of the Brazilian company Mylner for US$ 15.7 million (BRL 27.1 million). Frutarom paid a further BRL 4.4 million for Mylner's cash balance. The acquisition was completed upon signing.

Founded in 1974, Mylner develops, manufactures and markets flavor solutions, mainly sweet flavors for beverages and baked goods, natural plant extracts and natural flavor products. Mylner has a modern development, production and marketing site near

Sao Paulo, Brazil and its wide customer base includes leading food and beverage manufacturers located mainly in Brazil and other developing countries in Latin America. The acquisition allowed Frutarom to strengthen and deepen its presence and market share in the important Brazilian market while expanding its product offerings and its R&D and sales and marketing platforms, reinforcing its local production potential and improving service to customers in the region.

Sales turnover for Mylner for 2011 amounted to US$ 11.4 million (19 million Real), an 8% growth compared with 2010 when sales totaled US$ 10 million (17.5 million Real).

For further information regarding the acquisition of Mylner, see the Company's immediate report published on February 7, 2012 and Note 5(c) to the financial statements.

1.8.4. **Acquisition of JannDeRee** – On May 2, 2013 Frutarom signed an agreement to acquire 100% of the share capital of the South African flavors company JannDeRee for US$ 5 million. The acquisition was completed upon signing.

JannDeRee, founded in 1993, develops, manufactures, and markets flavors with an emphasis on savory flavors and sweet flavor solutions. Having grown rapidly in recent years, JannDeRee has a development, production and marketing site in Johannesburg, South Africa. JannDeRee also has a wide customer base in South Africa and other important developing countries in the sub-Sahara region such as Malawi, Zimbabwe and Mozambique. JannDeRee's activity is synergetic with Frutarom's activity in the field of flavors in African countries, activity which has grown at a faster pace than the rate of market growth over the past few years.

JannDeRee's sales in 2012 amounted to US$ 5 million.

During the third quarter of 2013 the merging of Frutarom's activities in South Africa was completed. This included the consolidating of Frutarom's South African activities at the JannDeRee site along with the integration of management and the purchasing, production, supply chain, R&D and sales and marketing functions.

For further information regarding the acquisition of JannDeRee, see the Company's immediate report published on May 2, 2013 and Note 5(d) to the financial statements.

1.8.5. **Acquisition of PTI** – On November 18, 2013 Frutarom signed an agreement for the acquisition of 75% of the share capital of the Cypriot company Vantodio Holdings Limited ("Vantodio"), owner of the Russian PTI group, for US$ 50.3 million (according to an enterprise value of US$ 67 million). The acquisition agreement included a mutual option for the purchase of the remaining 25% of Vanotodio shares by Frutarom from the end of the third year until the end of the fifth year based on a multiplier of between six and seven on the average EBITDA achieved over the three years preceding the option exercise and on other performance factors. The acquisition was completed on November 20, 2013.

PTI, established in 1996, engaged in the development, manufacture and marketing of unique and innovative savory solutions including flavors, spice mixes and functional ingredients for the food industry (including specialty protein-based ingredients produced through advanced technology), with special focus on processed meat and convenience foods. PTI also has trade and marketing activity, providing ingredients manufactured by others as part of the services it offers customers in furnishing comprehensive solutions.

Frutarom's is taking action to capitalize on PTI's R&D, marketing and sales infrastructure in Russia and in Central and Eastern European markets where it operates, as well as its own global sales and marketing infrastructure, in order to leverage and realize the many cross-selling opportunities this acquisition brings by expanding both the customer base and its product portfolio. Over recent months, according to plan, Frutarom combined its activities with those of PTI in countries where both companies operate, exploiting synergies between the activities and achieving operating savings. The acquisition enabled Frutarom to reinforce and deepen its presence and market share in the key markets of Eastern Europe while expanding its product offerings and its R&D and sales and marketing platforms, reinforcing its local production potential and improving service to customers in the region. Through this acquisition, Frutarom became one of the only global manufacturers with a substantial production site in Russia and possessing one of the top R&D, sales, marketing and distribution infrastructures in the region in its industry. Also contributing to raising Frutarom's market share in the region were sanctions imposed on the importing foodstuffs into Russia, changes in the exchange rates of local currencies, and a preference by consumers for buying locally-made products.

For further information regarding the acquisition of PTI, see the Company's immediate reports published on November 18 and 20, 2013 and Note 5(e) to the financial statements.

1.8.6. **Acquisition of Aroma** – On November 25, 2013 Frutarom signed an agreement for the acquisition of the entire share capital of the International Aroma Group, a Panamanian company holding the Guatemalan Aroma group, for a net cash payment of US$ 12.5 million (US$ 13 million less Aroma's balance of cash and cash equivalents amounting to US$ 0.5 million). A future payment mechanism in the purchase agreement provided for an additional sum equal to the EBITDA in excess of US$ 2.25 million achieved over the years 2013 to 2015 under which the Company paid an additional US$ 0.5 million in 2014. The transaction was completed upon signing.

Aroma, established in 1990, engaged in the development, manufacture and marketing of flavor solutions, including mainly sweet flavors for beverages, dairy products, sweets, snacks and convenience foods. Aroma has a production, development and marketing site in Guatemala City and a wide customer base which includes leading international food and beverage manufacturers as well as local food and beverage manufacturers in Guatemala, Honduras, Costa Rica, El Salvador and other developing countries, mainly in the region of Central America.

The acquisition allowed Frutarom to strengthen and entrench its presence and market share in the important markets of Central and South America while expanding its product offerings and enlarging its R&D, sales and marketing infrastructure, strengthening local production capabilities and improving customer service in the region.

For further information regarding the acquisition of Aroma, see the Company's immediate report published on November 25, 2013 and Note 5(f) to the financial statements.

1.8.7. **Acquisition of Hagelin** – On December 11, 2013 Frutarom signed an agreement for the acquisition of 100% of the share capital of the US based Hagelin in return for US$ 52.4 million. The acquisition was completed upon signing.

Hagelin, founded in 1967, develops, produces and markets flavors and unique flavor technologies for the food industry, with a focus on the growing area of beverage flavors. Hagelin also specializes, among other things, in the development of advanced flavor technologies in the areas of sodium reduction, sugar and calorie reduction and flavor enhancement, and its customer base includes leading international food and beverage manufacturers as well as local food and beverage manufacturers in the US, the UK and in emerging markets exhibiting high growth rates, mainly in Central and South America and Africa.

Hagelin’s activities in the UK have been integrated with Frutarom’s activity in that country, and Frutarom is taking steps to consolidate its activity with Hagelin’s activity in the US and capitalize on the many synergies this acquisition has generated in whatever areas.

For further information regarding the acquisition of Hagelin, see the Company’s immediate report published on December 12, 2013 and Note 5(g) to the financial statements.

1.8.8. **Acquisition of CitraSource** – On February 24, 2014 Frutarom acquired the American company CitraSource, whose assets include, among others things, a plant for processing specialty citrus ingredients, intangible assets and inventory, as well as a refrigerated tank farm used by CitraSource in its ongoing activities. The acquisition was made in return for a cash payment of US$ 7.5 million and also includes additional future consideration based upon CitraSource’s results for 2014-2018.

CitraSource, founded in 2003, specializes in research and development, production, marketing and the sale of specialty citrus solutions to leading international customers in the flavor and fragrance and food and beverage markets. CitraSource customers include leading global flavors and food and beverage producers. CitraSource's longstanding knowhow and excellent capabilities in producing unique substances and flavors from a variety of citrus sources (particularly oranges, lemons, grapefruits, and tangerines) are helping Frutarom to expand its natural products portfolio. CitraSource also has global purchasing capabilities in citrus and, in combination with Frutarom’s capabilities, further strengthen Frutarom's position as a leading player in R&D, production and sales of specialty citrus solutions which are an important component in the development and production of many flavors and food and beverage products.

Sales for CitraSource in 2013 amounted to US$ 7 million.

For further information regarding the acquisition of CitraSource, see the Company’s immediate report published on February 25, 2014 and Note 5(h) to the financial statements.

1.8.9. **Acquisition of Montana Food** – On November 28, 2014 the Company completed the acquisition of Montana Food, the flavors and natural food colors division of the Peruvian company Montana S.A, for a cash payment of US$ 24.9 million plus the assumption of US$ 7.1 million in debt.

The purchase agreement includes a mechanism for future consideration under which an additional payment will be made in the amount of twice the improvement in gross profit of the acquired activity beyond the current gross profit over the 18 months following the closing of the transaction. Montana Food has assets valued at US$ 24.8 million.

Montana Food is one of South America's leading companies in the field of flavors and natural food colors. Its customers include some of the world's leading global food, beverages and flavor companies as well as manufacturers based locally in South America and Central America.

In addition to its flavors and natural colors activities which constitute its core business and reached US$ 29.5 million in sales in 2013, Montana Food also engages in trade and marketing activity through which, as part of its service and the providing of comprehensive solutions to its customers, it markets ingredients that it does not produce itself.

Montana Food maintains an R&D, sales and marketing center and a modern, efficient production site in Lima, Peru with substantial capacity and the possibility for further extensive output expansion. The acquisition also included Montana Food's activity in Chile which includes an R&D and marketing center and a sales team for the Chilean market.

Following the acquisition Frutarom became the only global player in its field with a sizable production site in Peru as well as having one of the top R&D, sales, marketing and distribution platforms in the region.

Frutarom is working towards utilizing and integrating the R&D, sales and marketing infrastructure of the acquired activities with Frutarom's global R&D, sales and marketing infrastructure in order to leverage and capitalize on the abundance of cross selling opportunities generated by the acquisition, both through expanding the customer base and expanding the product portfolio. The acquisition also constitutes a major boost to Frutarom's global activity in the growing field of natural food colors and it intends to leverage Montana Food's capabilities and invest towards substantially expanding its activity.

For further information regarding the acquisition of Montana Food, see the Company's immediate reports published on September 30, 2014, October 14, 2014 and November 29, 2014 and Note 5(i) to the financial statements.

1.8.10. **Acquisition of Vitiva** – On February 4, 2014 Frutarom completed the purchase of 92% of Vitiva's share capital which grants it the right to acquire the balance of Vitiva's share capital, in exchange for payment of US$ 10.0 million for Vitiva's entire share capital.

Vitiva specializes in the research and development, production, marketing and sales of specialty natural extracts from plants exhibiting antioxidant activity or scientifically proven health attributes backed up by clinical studies and of natural colors for customers in the food, pharmaceutical, nutraceutical, and cosmetics markets. Among its customers are some of the world's top food, pharmaceuticals, and cosmetics manufacturers.

Vitiva has many years of experience and excellent capabilities in extracting active elements from plants (particularly rosemary, olive and citrus, among others) and this will help Frutarom expand its portfolio of natural products for the food industry as well as in the fields of health and cosmetics. In addition, Vitiva has R&D abilities and a pool of knowledge based on longstanding research for continuing to expand its current product portfolio and toward entry into other fields such as the field of pet food and livestock feed preservation. The natural food colors activity will join the natural food colors activity of Montana Food which was acquired by Frutarom in September 2014, advancing the implementation of Frutarom's strategy of penetration into this burgeoning field with the intention of continuing to invest in a major expansion of its global activity in this growing area.

Vitiva has an R&D, marketing and sales center and a modern, efficient production site in Slovenia with large output capacity along with the possibility for significant expansion.

For further information regarding the acquisition of Vitiva, see the Company’s immediate reports published on December 23, 2014 and February 4, 2015 and Note 22(a) to the financial statements.

1.8.11. **Acquisition of Ingrenat** – On February 2, 2015 Frutarom purchased 100% of the share capital of the Spanish company Ingrenat in exchange for payment of approximately US$ 8 million (€ 7 million) and up to approximately an additional US$ 1.1 million (€ 1 million) conditional upon Ingrenat's 2015 performance.

Ingrenat specializes in the research and development, production, and sales and marketing of natural extracts from plants which include, among others, paprika, rosemary, bixin, alfalfa and more which deliver taste, color, and antioxidant activity solutions for the food industry. Numbering among its customers are food manufacturers and leading flavor, fragrance, and natural color producers.

Ingrenat's sales rose by 10% in 2014 to US$ 9.8 million (€ 7.4 million). The acquisition of Ingrenat is a continuation of the implementation of Frutarom's strategy of deepening and expanding in the areas of natural food colors and antioxidants and it will continue investing towards substantially expanding its global activity in these important and growing fields. The natural food colors activity joins the natural colors activity of Montana Food and Vitiva. Ingrenat's activity in antioxidants, particularly in the field of food protection and shelf life extension based on natural substances, further reinforces Frutarom's line of solutions in this area which also gained a substantial boost with the acquisition of Vitiva which has activity in this growing field as well.

Ingrenat has an R&D and sales and marketing center, and a production site in Murcia, Spain with large production capacity and the possibility of extensive expansion, of which Frutarom will look to gain full advantage and achieve significant operational savings. Frutarom will also work towards realizing the cross-selling opportunities inherent in the acquisition.

For further information regarding the acquisition of Ingrenat, see the Company's immediate report published on February 3, 2015 and Note 22(c) to the financial statements.

1.8.12. **Acquisition of FoodBlenders** – On February 3, 2015 Frutarom purchased 100% of the share capital of UK-based flavors company FoodBlenders in exchange for payment of approximately US$ 2.4 million (£ 1.6 million) plus an additional amount conditional on performance which is expected to stand at US$ 600,000 (£ 400,000).

Established in 1998, FoodBlenders develops, manufactures, and markets savory solutions which mainly include spice and seasoning mixes, functional ingredients, marinades and sauces for the food industry, with particular emphasis on the convenience foods segment. Sales for FoodBlenders amounted to US$ 3 million (£ 2 million) in 2014.

FoodBlenders has a site in England where it develops, manufactures and markets its products which is located in close proximity to Frutarom's Wellingborough site, and it has a wide customer base which includes British food and private label manufacturers.

FoodBlenders' product line and technologies complement the product portfolios and activities of UK-based Savoury Flavours and EAFI which were acquired by Frutarom in 2012 and 2011 respectively and which also specialize in savory flavor solutions. The proximity to the Frutarom site at Wellingborough and the complementary line of products promise to generate synergies between FoodBlenders' activity and Frutarom's expanding savory activity in the UK and throughout the world.

For further information regarding the acquisition of FoodBlenders, see the Company's immediate report published on February 3, 2015 and Note Note 22(b) to the financial statements.

The consolidation trend in the industry in which Frutarom operates is continuing. Numbering among the world's top 10 companies in flavors and specialty fine ingredients,[3] Frutarom continues to be one of the leading and most active companies in the market in performing acquisitions. Frutarom's management will continue investing substantial resources in locating and pursuing more potential new acquisitions which suit its strategy of rapid and profitable growth.

The Company believes that its robust equity structure, the strong cash flow it generates and the backing it enjoys from leading financial institutions will enable it to continue implementing its acquisitions strategy.

2. ***The Group's Fields of Operation***

2.1. Frutarom is a global company that develops, manufactures, markets and sells comprehensive solutions with respect to the flavors and specialty fine ingredients used in the production of food and beverages, flavors and fragrance essences, pharmal/nutraceutical products, cosmetics, personal care and other products.

2.2. Frutarom has two main activities, each constituting a main field of operations which is reported as a business segment in the Company's consolidated financial statements (see also Note 6 to the financial statements) and considered by Company management as being Frutarom's **core businesses**:

2.2.1. **Flavors activity** – In the framework of its Flavors activity, Frutarom develops, produces, markets and sells sweet and savory flavor solutions, including flavoring additives, functional products, natural colors for food, and products also containing, in addition to flavor additives, elements of fruits or vegetables or other natural substances (food systems) used mainly in the manufacture of food and beverages and other consumer products. Frutarom develops thousands of different flavor solutions for its customers, most of them tailor-made to the needs of the specific customer. Frutarom also engages in developing new products and adapting them to changing consumer preferences and to future customer requirements.

Frutarom's Flavors activity expanded rapidly and profitably by combining organic growth and acquisitions, and now constitutes 72% of Frutarom's total sales (compared with 33% in 2000). This

[3] Source: Leffingwell & Associates, October 2014

accelerated growth is the result of focusing on the fast growing field of natural flavors, developing innovative unique solutions combining taste and health for the large multinational market sector, focusing on mid-size and local customers in developed and emerging markets with special focus on private label customers and emphasizing customized service for their particular needs which includes technological and marketing support, assistance in product development support and offering a high level of service and tailor-made solutions as are normally provided to large multi-national customers, and the result of strategic acquisitions which were and are still being successfully integrated with Frutarom's global activities.

2.2.2. **<u>The Specialty Fine Ingredients activity</u>** – As part of its Specialty Fine Ingredients activity, Frutarom develops, produces, markets, and sells natural flavor extracts, natural functional food ingredients, natural pharma/nutraceutical extracts, natural algae-based biotech products, natural antioxidants for food protection solutions, aromatic chemicals, essential oils, specialty citrus products, and natural gums and resins. The specialty fine ingredient products are sold principally to the food and beverage, flavor and fragrance, pharma/nutraceutical, cosmetics and personal care industries.

Frutarom focuses its Specialty Fine Ingredients activity on a portfolio of high added-value products which gives it a competitive advantage. Most of the specialty fine ingredient products in taste and health are natural products for which demand is growing at a higher average rate than for products which are not natural. In recent years Frutarom has been focused on expanding the portfolio of natural ingredients offered to customers, with special emphasis on the field of natural, functional and health foods. Specialty Fine Ingredients activity accounted for 18% of total Frutarom sales in 2014.

2.3. In addition to its core activities, Frutarom also engages in importing and marketing various raw materials that it does not itself manufacture as part of the service and extending of comprehensive solutions that it provides its customers. This trade and marketing activity is synergetic and supportive of Frutarom’s core activities, leveraging its sales, supply chain, and purchasing platforms and global management system, and allows Frutarom to offer a wider variety of products solutions and added value to its customers, particularly those of medium size and locally based, and to deepen cooperation with such customers. This activity, which was expanded following the acquisitions of Etol, PTI and Montana Food, centers mainly on Central and Eastern Europe, Latin America and Israel. Sales from this activity constituted 10% of total Frutarom turnover in 2014.

2.4. Frutarom's growth strategy is based on identifying the future trends in consumer preferences and in the food and beverage markets, and adjusting its activity accordingly to quickly provide its customers comprehensive solutions that address consumer demand and preferences. Recent years have seen a rapid shift by food and beverage companies to the use of natural flavors, ingredients and colors, with particular focus on functional foods and on reduced fat, sodium and sugar products, as well as clean-label products, that are viewed as having healthier and more nourishing and environmentally friendly qualities. This shift has also been due to the evolving of regulatory standards in many countries throughout the world that limit the use of certain substances and lead to improved nutritional properties in foods and beverages, resulting in manufacturers needing to employ innovative technologies and solutions based on natural products. Consumer awareness towards proper and healthy nutrition has not compromised demand that products remain tasty despite less sugar and salt being used and the addition of healthy ingredients that often leave an aftertaste.

Another notable trend over recent years is a rise in the number of hours the average consumer spends outside the home and, as a result, growing demand for ready-made and convenience food that is both tasty and healthy. This trend is supported by the rise in the scope of disposable income for consumers and their willingness to increase their spending on processed foods and convenience products, and on products perceived as healthier. A continuing trend of demand by consumers for healthier and more natural food can be seen in developed markets, and increasingly in emerging markets as well. Frutarom has identified these trends and uniquely positioned itself as a supplier of comprehensive solutions combining taste and health. Maximizing the synergies between its varied activities enables Frutarom to offer its customers excellent scientifically-based taste solutions along with added health qualities, with emphasis on the use of natural ingredients. The combination of its various activities also allows Frutarom to provide its customers with solutions for improving texture and prolonging the shelf life of their products (important qualities for processed food manufacturers in the production of convenience food) based on the inclusion of innovative, natural ingredients.

2.5. The ability to offer the comprehensive solutions in the fields of flavors and health (as shown by the diagram below) means substantial added value for Frutarom customers, giving the Company a strategic advantage and differentiating it from its competitors.

Customer in the Center

3. <u>Investments in the Company's Capital and Transactions in its Shares</u>

3.1. To the best of the Company's knowledge, no material investments in the Company’s capital or any material transactions in the Company's shares were performed outside the stock exchange during the years 2013-2014 by any interested party in the Company.

3.2. For further information regarding self-purchase of the Company’s shares as part of the compensation plans for Company employees, see Note 12(b) to the financial statements.

4. <u>Distribution of Dividends</u>

4.1. Over the past two years the Company announced and distributed dividends to its shareholders as follows:

Year	Dividend Per Share (NIS)	Total Sum (NIS 000's)	Total Sum (US$ 000's)	Distribution Date
2013	0.24	13,886	3,892	May 5, 2013
2014	0.28	16,292	4,712	May 4, 2014

The above-stated dividend distributions did not require court approval.

4.2. Distributable retained earnings as of December 31, 2014 amount to US$ 445,653 thousand. Upon approval of the financial statements for the period ended December 31, 2014, the Board of Directors declared a dividend of NIS 0.38 per share, a 35.7% increase over the previous year's dividend.

4.3. The Company does not have a dividend distribution policy. The Company's decisions on distributing of dividends depend on several factors including the Company's level of profitability and its investment and strategic acquisitions plans, among others. The Company intends to continue distributing dividends to its shareholders in the future as well. However, there can be no certainty that any such dividend will be declared and distributed in the future or that any dividend distributed in the future will be in accordance with the above.

4.4. On February 16, 2012 the Company undertook limiting its distribution of dividends in the framework of a revision to its financial covenants, which will permit it to distribute:

(A) Up to 50% of retained earnings accumulated up to December 31, 2011 as presented in the Company’s 2011 balance sheet.

(B) Up to 50% of the Company’s annual net income in each calendar year as presented in the Company’s financial statement relating to the same calendar year in which this income was accrued.

For further information, see the Company’s immediate report dated February 16, 2012.

CHAPTER 2 – OTHER INFORMATION

5. *Financial Data Regarding the Company's Fields of Activity*

5.1. In 2014 Frutarom's sales rose 21.6% to reach an annual sales record of US$ 819.5 million, compared with US $673.7 million in 2013. For a breakdown of Frutarom's sales by field of activity, see section C to the Board of Directors' discussions of the Company's state of business in the Directors' Report (Results of Operations in 2014).

5.2. Following are the Group's financial figures for 2012 through 2014 by field of activity:

2014 (US$000)		Field of activity		Consolidation Adjustments	Total core business	Trade & Marketing	Consolidated
		Flavors	Fine Ingredients				
Sales	From external customers	589,763	151,264	-	741,027	78,520	819,547
	From other fields of activity	-	7,111	(7,111)	-	-	-
Total Sales		589,763	158,375	(7,111)	741,027	78,520	819,547
Expenses	Expenses constituting sales for other fields of activity	7,111	-	(7,111)	-	-	-
	Expenses not constituting sales in other fields of activity	485,447	138,885	450	624,782	75,841	700,623
Total Expenses		492,558	138,885	(6,661)	624,782	75,841	700,623
Operating Income [4]		97,205	19,490	(450)	116,245	2,679	118,924
Operating income attributed to non-controlling interests		1,174	444	-	1,618	-	1,618

[4] Total consolidated operating income includes operating income attributed to non-controlling interests.

2013 (US$000)		**Field of activity**		**Consolidation Adjustments**	**Total core business**	**Trade & Marketing**	**Consolidated**
		Flavors	**Fine Ingredients**				
Sales	From external customers	494,389	139,597	-	633,986	39,707	673,693
	From other fields of activity	-	5,994	(5,994)	-	-	-
Total Sales		494,389	145,591	(5,994)	633,986	39,707	673,693
Expenses	Expenses constituting sales for other fields of activity	5,994	-	(5,994)	-	-	-
	Expenses not constituting sales in other fields of activity	419,641	128,354	150	548,145	38,791	586,936
Total Expenses		425,635	128,354	(5,844)	548,145	38,791	586,936
Operating Income [5]		68,754	17,237	(150)	85,841	916	86,757
Operating income attributed to non-controlling interests		232	618	-	850	-	850

2012 (US$000)		**Field of activity**		**Consolidation Adjustments**	**Total core business**	**Trade & Marketing**	**Consolidated**
		Flavors	**Fine Ingredients**				
Sales	From external customers	457,341	138,318	-	595,659	22,342	618,001
	From other fields of activity	-	2,445	(2,445)	-	-	-
Total Sales		457,341	140,763	(2,445)	595,659	22,342	618,001
Expenses	Expenses constituting sales for other fields of activity	2,445	-	(2,445)	-	-	-
	Expenses not constituting sales in other fields of activity	395,419	128,385	7	523,811	21,342	545,153
Total Expenses		397,864	128,385	(2,438)	523,811	21,342	545,153
Operating Income [5]		59,477	12,378	(7)	71,848	1,000	72,848
Operating income attributed to non-controlling interests		-	621	-	621	-	621

5 Total consolidated operating income includes operating income attributed to non-controlling interests.

5.3. Nature of consolidation adjustments: Intercompany purchases, sales, and profits and losses are eliminated in adjusting for consolidated results.

5.4. Explanation of developments: For an explanation on developments occurring in the data shown above, see the explanations appearing in the Directors' Report for the year ended December 31, 2014.

5.5. Allocation of costs shared jointly by the Flavor and Specialty Fine Ingredients activities is performed on the site level where resources are shared between both activities and according to the relevant load parameters for each of the shared resources. Any change to the load parameters requires preapproval from Group headquarters. There have been no significant changes in the allocation rates for shared costs in recent years.

6. Market Environment and the Effect of External Factors on Company Activity

Market Environment – Global Flavor and Fragrance Industry

Frutarom operates in the global flavors and specialty fine ingredients markets.

6.1. The global market for flavors, fragrances, and raw materials for these industries was estimated at US$ 23.9 billion[6] for 2013. Frutarom does not operate in the fragrance market but does operate in the natural functional food ingredients market as well as the natural colors market (which are not included in the above estimate). Accordingly, the Company believes that the scope of sales in the markets in which it operates stands at approximately US$ 23 billion. Based on data from Leffingwell & Associates, Frutarom ranks among the top ten companies worldwide in the field of flavors and fragrances.

6.2. Market research firm IAL Consultants[7] projects sales in the flavors markets of industrialized countries (the USA and Western Europe) growing at an annual rate of about 2.4% from 2013 to 2018. According to these projections, the growth rate in emerging markets such as Asia, Central and South America, Eastern Europe and Africa is expected to be higher as a result of changes of consumer preferences in these markets and a shift to processed foods, and may reach an average annual rate of 4.0% between 2013 and 2018.

---

[6] Leffingwell & Associates, January 2015
[7] IAL Consultants, January 2015

6.3. It is common to view the Flavor and Fragrance (F&F) market as a single integral market. Manufacturers operating in the F&F market can be broken down into three main groups: 1. Large global companies; 2. Medium sized global companies; 3. Small and locally-based companies.

The large global companies operate throughout the world and have sales turnover of over US$ 2.5 billion. There are four such companies in the global F&F market: Givaudan, Firmenich, IFF Inc. and Symrise; and they generally focus on large multinational food and beverage manufacturers. Based various assumptions and on on figures published by Leffingwell & Associates, it is believed this group represents about 55% of the market.

The medium-sized global companies, Frutarom among them, generate between US$ 400 million and US$ 2.5 billion in revenues. There are about eight medium-sized companies in the global F&F market, some having primarily a regional focus (such as Japan) while some like Frutarom operate in the global market. This group is believed to make up about 25% of the market based on various assumptions and on figures published by Leffingwell & Associates.

It should be pointed out that the vast majority of small locally-based companies, which have sales turnover of less than US$ 400 million, are much smaller with sales ranging from several million to several tens of millions of US dollars. These companies generally focus on small local customers and have limited capabilities in the areas of R&D, innovation, and for providing customized services to their customers. This group numbers over 800 companies and is believed to make up about 19% of the market based on various assumptions and on figures published by Leffingwell & Associates.

6.4. The flavors and fine ingredients market in which the Company operates is characterized by high entry barriers such as:

- Long-term relationships: The market is characterized by long-term relationships between manufacturers and their customers, which include mostly the food and beverage, flavor and fragrance extracts and pharmaceutical/nutraceutical industries. Much importance is given in these industries to supplier reliability, quality of service, and the manufacturers' understanding of their customers' needs.
- Research and development: Since end user preferences are constantly changing and the markets in which customers operate are dynamic and competitive (particularly the foods and beverages market), the market is characterized by an abundance of new and innovative products. Manufacturers therefore need to invest heavily in R&D and offer a wide range of new products, either at the initiative of the flavor manufacturer or in collaboration with the customer (the food or beverage manufacturer) at the customer's initiative.

- Compliance with quality and regulatory standards: Flavor and fine ingredients products are mainly intended for use by the food and beverage and pharmaceutical/nutraceutical industries which are subject to strict quality and regulatory standards. Manufacturers are therefore required to meet the same strict standards. Recent years have seen a trend towards increasingly stringent quality and regulatory standards which could even further impair the competitiveness of small flavors manufacturers and raise the entry bar to new players.
- Importance of flavorings in the final product: Flavor additives determine the taste of the end product and therefore play a critical role in its success. Moreover, flavor additives cannot be precisely replicated and their cost is marginal compared with the end product's overall cost, so customers tend to avoid switching flavor manufacturers.
- Investment in production capacity for ingredients: Considerable capital investment is required for building up production capacity for ingredients. Such investment constitutes a significant entry barrier for new manufacturers in the industry.

In light of the entry barriers described above, penetration into the market by new manufacturers is mainly accomplished through mergers and acquisitions. Overall, the market is in the process of consolidation and a diminishing number of manufacturers.

CHAPTER 3 – DESCRIPTION OF THE COMPANY'S BUSINESS BY FIELD OF ACTIVITY

6.5. Frutarom is a global company that develops, manufactures, markets and sells comprehensive solutions in the field of flavors and specialty fine ingredients used in producing foods, beverages, flavor and fragrance extracts, pharma/nutraceuticals, cosmetics, and personal care and other products. Frutarom has two principal fields of operation, each constituting a main field of activity: Its Flavors activity and its Specialty Fine Ingredients activity. The Company considers these activities as constituting its core business.

6.6. In addition to its core activities, Frutarom also engages in the import and marketing of various raw materials that it doesn't produce on its own as part of the service and providing of comprehensive solutions to its customers. The trade and marketing activity is synergetic and supportive to Frutarom’s core business, leveraging its sales, supply chain, global purchasing, and management systems. This allows the Company to offer its customers, particularly those in emerging markets that are medium-sized or locally-based, a wider variety of products, solutions, and added value and to deepen its partnership with these customers. This activity was expanded following the acquisitions of ETOL, PTI and Montana Food, and is focused mainly towards Central and Eastern Europe, Latin America and Israel.

6.7. The Company’s various activities are largely complementary and synergetic. This synergy is expressed in a number of areas:

- Sales and marketing: Frutarom's sales and marketing policy is having a single dedicated salesperson work with each customer and providing sales services for the full range of Frutarom products. Specialty Fine Ingredients activity products to the food and beverage industry are sold through the Flavors activity's sales personnel. The Trade & Marketing activity also plays a complementary role by leveraging Frutarom’s sales, supply chain, and global purchase systems, allowing Frutarom’s other activities to offer comprehensive solutions to customers.

- Research and development: The knowhow of the personnel in the Flavors activity and their familiarity with the needs in the food and beverage market customers enables the Company to develop new and innovative specialty fine ingredients for the food and beverages industry.

- Operations: Some of Frutarom's production sites and part of its supply chain system are jointly used by Frutarom’s different activities which share their resources.

- Specialty Fine ingredients: Most of the specialty fine ingredients produced by Frutarom are sold to third parties. However, part of the fine ingredients is used by Frutarom's own Flavors activity, and some is used exclusively by Frutarom for the development and production of unique taste and health solutions, giving the Company a competitive advantage.

In light of the considerable synergy between its activities and Frutarom's focus on providing comprehensive solutions combining flavor solutions and specialty fine ingredients, some possessing healthful qualities, along with ingredients for helping create texture and richness of the food product, it is not always possible to separate the fields of activity on the basis of their various attributes.

Flavors Market

7. Overview of the Flavors Market

General

7.1. Flavor products are the key foundations for providing taste in processed foods and beverages, and as such play a significant role in determining consumer acceptance of the end products in which they are used.

7.2. In the estimation of market research firm IAL Consultants,[8] 2013 global sales in the field of flavors amounted to approximately US$ 11.6 billion. Flavor products are sold primarily to manufacturers of prepared foods, beverages, dairy products, bakery products, processed meat and fish products, confectionery products, oral hygiene products, pharmaceuticals, animal feed and tobacco products.

7.3. The global market for flavors has expanded rapidly over the last 60 years, mainly the result of growing demand as well as an increasing variety of consumer end products containing flavors. Increasing demand for consumer goods containing flavor products is due to global population growth along with changing consumer preferences resulting from rising personal income, demographic changes, the rise of leisure pastimes, growing awareness of health issues and urbanization. These factors have led to an overall increase in the number of food and beverage products containing flavor additives and to significant growth in demand for convenience foods and products containing natural and healthy elements.

[8] IAL Consultants, January 2015

7.4. The following table shows 2013 sales in the flavors market by geographic region and their projected average annual growth rates:[9]

Region	Estimated world consumption in 2013 (US$ million)	Average annual growth expected for 2013-2018
Western Europe	2,187	2.4%
Eastern Europe	946	3.0%
North America	2,583	2.9%
South & Central America	1,277	3.6%
Asia	3,885	4.8%
Middle East and Africa	727	4.7%
Total	**11,605**	**3.7%**

7.5. According to the above estimates, the largest market in flavors in 2013 was Asia which accounted for 33.5% of the global market, followed by North America with 22.3%. With regards to growth rates projections for 2013 to 2018, the Asian market is expected to grow the fastest (4.8%) followed by the African and Middle Eastern market with an expected annual growth rates of 4.7%.

Frutarom has successfully increased its penetration into the growing markets of Asia, North and South America, Eastern Europe, the Middle East and Africa, and will continue to work towards accelerating its penetration into these markets by, among other things, focused strengthening of its R&D, production, marketing and sales platforms in important target countries, taking advantage of the synergies from acquisitions completed over the past few years, along with continuing to carry out further strategic acquisitions. The Company is also working towards continuing to expand its activity in Western European markets by leveraging its broad product portfolio and continuing to capitalize on its cross-selling opportunities.

Characteristics of the Flavors Market

7.6. Reliable and quality service: Food and beverage producers, the main customers of flavor manufacturers, expect reliable and quality service to meet their needs in terms of support and lead time while also maintaining high quality, regulatory standards, and strict safety criteria. These expectations entail the formation of long-term relationships between flavor producers and their customers. As a result, large multinational customers as well as more and more medium-sized customers have been steadily reducing the number of

[9] IAL Consultants, January 2015

their flavor suppliers to a select list of authorized suppliers, thereby creating an entry barrier for small flavor manufacturers.

7.7. Research and development: Development of flavor products in general and of new flavor extracts in particular is a complex, creative and technological process that calls for knowledge and many skills on the part of a flavor manufacturer's R&D personnel. Effective R&D is critical in ensuring a continuous stream of innovative new products and in maintaining profitability and growth for any flavor manufacturer.

The initiative for developing new flavor products can originate from the flavor manufacturer itself or from a customer in need of a certain flavor for an end product under development. So in order to anticipate market demand, the flavor manufacturer's R&D team needs to be very familiar with taste preferences in target markets as well as with the end products. In addition, as most flavors are tailor made for specific customers, close cooperation with the customer is required. The formulas for these flavor products are commercial secrets, usually remaining the property of the flavor manufacturer. Since most flavor products are customized for the needs of the specific customer, the customer usually refrains from switching flavor suppliers over the lifespan of the end product.

7.8. Low price sensitivity: Since flavor products determine how the end product tastes, they play a vital role towards its success. Flavor products also cannot be precisely copied, and their cost compared to the overall cost of the end product is negligible. Therefore, when selecting a flavor supplier, the customer will place greater emphasis on the reputation, innovation, service, quality and consistency of the supplier than on the price of the flavors extracts, so demand for flavor products generally isn't very sensitive to changes in their price.

7.9. Production processes: Flavor products in general and flavor extracts in particular tend to contain many different ingredients (typically more than dozens of ingredients per flavor) which are blended according to unique formulas created by the manufacturer's R&D team. The production processes involved in the manufacture of flavor products are less complex and capital intensive than those used in producing fine ingredients, but producing flavor products demands skill and knowhow to achieve the required level of quality and consistency.

7.10. High and relatively stable profitability: As the flavors market tends to be characterized by long-term relationships and relatively low price sensitivity, along with relatively uncomplicated production processes, it generally enjoys high and stable profit margins (also in comparison to the fine ingredients market).

7.11. Entry barriers: For details regarding the entry barriers characterizing the flavor market, see section 6.4 above.

Characteristics of the Food and Beverage Market

7.12. The main customers of flavors manufacturers are food and beverage producers, and therefore the flavors market is generally driven by trends characterizing the demands and needs of the end consumers in the food and beverages market. According to Data Monitor, global sales in the food and beverage market amounted to US$ 4,784 billion in 2013.[10] Frutarom estimates that medium-sized, local and small food and beverage producers (having annual turnover of less than US$ 1 billion) comprise over than 60% of global sales. Although there has been a general trend towards consolidation in the food and beverage industry, Frutarom believes that mid- and small sized food and beverage producers and local food and beverage producers will continue to comprise a considerable share in this market and play a significant role.

7.13. The large flavor manufacturers (having annual sales turnover exceeding US$ 2.5 billion) tend to focus mainly on large multinational food and beverage producers, offering these customers a high level of service and the development of flavors specifically tailor-made to their needs. Frutarom believes these producers give less attention to medium-sized and local customers, offering such customers limited service, and do not devote many resources towards developing flavors customized to fit their needs. However, the Company believes medium-sized and local food and beverage producers require the same high level of service and the tailoring of products to their needs as the large multinational producers, as well as short lead times and flexibility in order quantities. Small and local flavor producers often do not have the product variety and service capabilities for providing the support needed to answer the varied needs of such customers. A specific example of this type of customer is the private label customer (see section 7.14 below). This situation creates a business opportunity for flavor producers not included in this group to focus more on servicing this large market segment. For details regarding Frutarom's Favors activity with medium-sized food and beverage producers, see section 8.3 below.

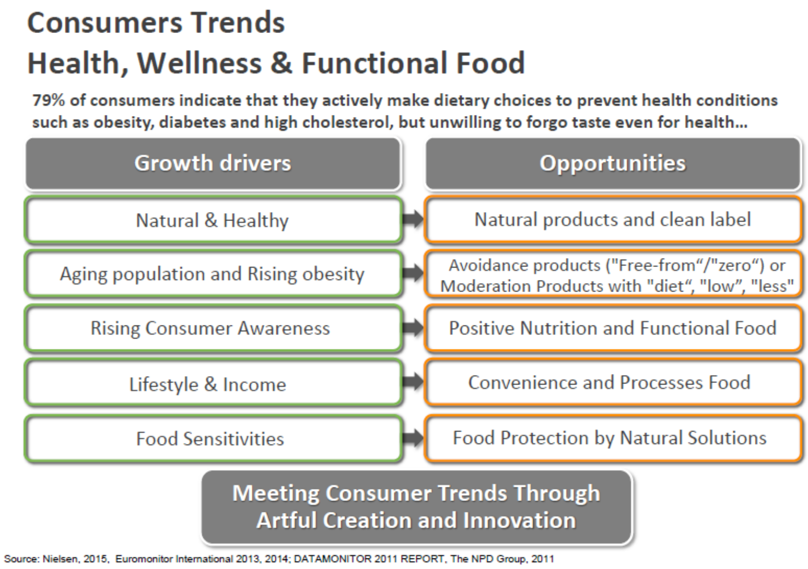
7.14. The food and beverages market is characterized by several main trends that affect the flavors market, as follows:

7.15. Local and global tastes: Taste preferences vary geographically and between different cultures so Flavor manufacturers must have a thorough knowledge of the local tastes in each of the countries where they operate. It is therefore important for a global flavor manufacturer to maintain a physical presence in its target markets and direct contact with local customers in order to understand local tastes and to be able to respond quickly and efficiently to changing consumer preferences. At the same time, globalization is also having an impact

[10] Feb, 2014 Datamonitor, Euromonitor and Frutarom's estimations

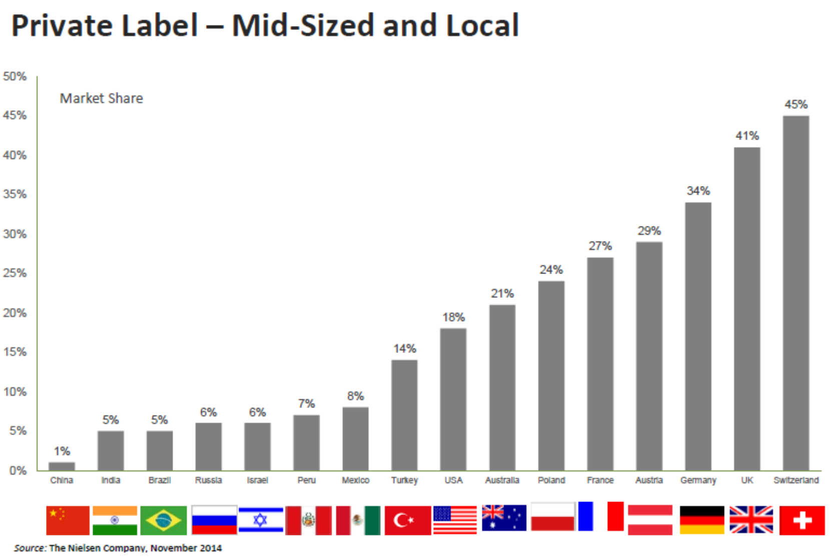
on the flavor industry as multinational food and beverage customers launch the same brand in a number of different markets simultaneously, often changing the taste profile to adapt it to the differing preferences of varied populations worldwide. For details regarding Frutarom's global geographic reach and familiarity with local flavors, see section 8.2 below.

7.16. Preference for natural products: Demand is on the rise for food and beverage products containing natural ingredients and possessing dietary and nutritional value (reduced fat, salt, sugar, etc.) since natural products are generally perceived by consumers as being of higher quality, healthier and more environmentally friendly. There has also been growing demand for "clean label" and organic products. As a result, natural food and beverage products are viewed as premium products that command higher prices. This trend has created new opportunities for flavor manufacturers in developing new and innovative natural flavor products that combine solutions for both natural colors and for use in natural substances for food protection solutions and extending shelf life. Frutarom focuses on developing and producing natural products and over two thirds of its products are now natural. In developed markets most of the growth derives from a shift by consumers to products considered healthier and more natural and their willingness to continue purchasing such products even during an economic slowdown.



7.17. Private label: Private label manufacturers, mostly medium-sized, local or small food manufacturers, constitute a growing segment in the flavor market. Over the last decade, with the strengthening of supermarket chains and growing consumer price consciousness, demand and consumption of private label products faster than for the brand food industry. This trend, which gained momentum in 2009 due to the global economic crisis, has continued over the following years as well and is expected to continue in the years ahead. Consumers who have tried out private label products tend to continue using them after enjoying a positive experience. In addition, the growing power of supermarket chains and their determination to increase their operating margins have led them to push towards strengthening their private label sales by, among other things, allocating large amounts shelf space and broadening the range of products. In markets where private labels are especially strong, such as Switzerland, Spain, the UK and Germany, their market share has reached 34% to 45%.[11] Supermarket chains, grocers and other retailers have also become aware of the importance of supporting their own private brand image. The demand from grocery chains and retailers for private label products that are similar to existing products in the market and distinctive premium products and their willingness to launch more innovative products has provided flavor and specialty fine ingredients manufacturers with new opportunities. We have also seen the beginning of a trend towards penetration by private labels in emerging markets as well. For example, from 2012 to 2014 private label activity in India rose by 27%.[12] Frutarom focuses on private label manufacturers and makes strategic cooperative ventures with them in which it provides them with a high level of added value by, among other things, offering marketing and technological support, the development of innovative products, and reduction in costs, and it intends to continue expanding its market share among these customers, both in emerging markets and in developed markets.

The following graph shows the rates of penetration by private label products in various countries:[13]



11 According to Statista.com 2015 – Private label market share in 2013 was 45% in Switzerland, 41% in Spain and the UK, and 34% in Germany.
12 The Nielsen Company, November 2014
13 The Nielsen Company, November 2014

7.18. Increasing consumption of convenience foods: Demand is on the rise for processed foods providing a greater degree of convenience (used both in home and away) such as "ready to eat" meals, fresh pasta, fresh ready-to-cook seasoned or marinated meat and poultry, salads and dressings. This has created new opportunities for flavor manufacturers, particularly those in the fields of savory flavors and functional fine ingredients which are responsible for giving food products their texture and extending their shelf life, to develop and market flavor products and specialty fine ingredients for this large market segment.

7.19. Emerging markets: Over the last few years the increase in consumption of flavored products in emerging markets, such as Asia, Central and South America, Central and Eastern Europe and Africa has been higher than the average growth rate for the global flavors industry. These markets have also been experiencing rising consumption of processed foods which has driven the growth of medium-sized, local and small food companies and created new market opportunities for flavor manufacturers. Frutarom expects that the continual shift to processed foods and changes in consumer habits in these markets will bring about continued growth in these markets at a higher rate than the expected pace of growth in developed markets.

Critical Success Factors in the Flavors Field

7.20. Company management believes that the critical success factors in the field of its flavor activities are:

- Long-term relationships – Long-term relationships with customers and collaboration in the development of new products;

- Global and local presence in target markets – Familiarity with the various taste preferences in the various markets and the ability to provide global and local support to customers. For details regarding Frutarom's expansive geographic reach, see section 8.2 below;

- Superior and reliable service – The flavor manufacturer's reliability and ability to provide first-rate service are critical for medium-sized and local customers as well as multinational customers;

- Presence in emerging markets – Many emerging markets are growing at considerably higher rates than developed markets, a presence in these key regions, an understanding of their special needs, and the ability to provide support to manufacturers in these markets all constitute critical success factors;

- Research and development and innovation – The ability to develop new products, whether at the flavor manufacturer's initiative or in collaboration with customers, has enormous importance;

- Compliance with quality, regulatory and safety standards – Since flavor extracts are intended mainly for the food and beverage and pharmaceutical markets, they must comply with strict quality, regulatory and safety standards;

- Purchase of raw material – It is becoming increasingly vital to allocate resources towards focusing on purchasing from countries which serve as important sources for numerous natural raw materials, such as China, India and Brazil, while expanding the circle of suppliers, maximizing the potential for reducing costs through a global purchasing system, and tightening ties with raw material manufacturers, processers and growers, particularly in the area of natural raw materials, in order to guarantee their continuous and reliable supply over time and to bring about improvement in purchase costs.

8. Products, Services and Added-Value Provided from Flavors Activity

Frutarom's Flavors activity, the most profitable of its activities, has been experiencing rapid growth since 2000. The Company's sales from flavors grew from US$ 26.5 million in 2000 to US$ 589.8 million in 2014.

This rapid growth is the result of (a) focusing on the fast growing area of natural food flavors; (b) the development of unique innovation-based solutions combining taste and health for the market segment of large multinationals; (c) focusing on mid-size and local customers in developed and emerging markets (with special focus on private label customers) with emphasis on providing them with services adapted to their particular needs including technological support, assistance in developing products, marketing support, and offering top-notch service and tailor-made products such as are normally provided to large multinational customers; and (d) the execution of strategic acquisitions which have and are being successfully incorporated into Frutarom's global activities.

8.1. The relative portion of the Flavors Activity as a percentage of Frutarom's overall activity grew from 33% in 2000 to 72% in 2014.

8.2. Since the success of many of the flavors produced by Frutarom depends on its familiarity with local tastes, The Company's Flavors activity maintains 34 R&D laboratories and 62 marketing and sales offices in close proximity to its customers in target markets. In addition, Frutarom's global spread enables it to introduce new tastes to local markets. Frutarom's global reach also allows it to fill the needs of food and beverage producers on launching global brands in various markets simultaneously.

8.3. Frutarom's Flavors activity provides an efficient, high quality solution towards the quick growth of its customers' private label products, providing assistance and support in developing the products and from a marketing perspective. Most private label manufacturers are medium-sized, local food and beverage producers. Frutarom offers such customers technological support, assistance in the development of products, marketing assistance, and a wide selection of products, along with service suited to their particular needs and flexibility in minimum order quantities and lead delivery times. Frutarom's acquisitions over the last few years have considerably expanded the portfolio of products that it can offer private label manufacturers and have expanded its global reach which allows it to be nearer to such customers.

8.4. Frutarom's Flavors activity offers a wide variety of flavor solutions designed to create new tastes, enhance existing tastes, and/or mask certain tastes in processed foods and beverages.

8.5. Most flavor products consist of numerous raw materials (flavors, for example, typically contain dozens of raw materials) combined according to unique formulas developed in Frutarom laboratories by the Flavors activity's R&D team. The development of a new flavor may be undertaken either at Frutarom's own initiative or based on specific requirements of its customers and in close collaboration with them. In addition, Frutarom can offer its customers solutions that include, besides flavors, natural functional ingredients that contribute to the product's nutritional value and the health of the consumer, help extend the product's shelf life, as well as natural colors (for more information, see section 13 below).

8.6. Frutarom's flavor products can be divided in different ways: by application (beverage, dairy, snacks, confection, processed meat and fish, etc.), by source of raw materials (natural, organic, artificial), by taste (sweet, savory), by form (liquid, powder, emulsion, granulated, paste), and by other methods.

8.7. Applications: The flavors produced by the Company are used primarily as ingredients in consumable goods manufactured by food and beverage producers and are suited for different types of applications such as soft drinks, juices, dairy products, ice cream, pastries, confectionery, chewing gum, and a variety of savory foods including snacks, convenience foods, ready-made soups, and salad dressings, as well as processed meat and fish, meat substitutes, pharmaceuticals and pet foods.

8.8. Source: Frutarom offers natural, organic, nature-identical and artificial flavor products. The natural flavors are produced strictly from natural ingredients which include, among other things, natural extracts and essential oils. Nature-identical and artificial products include synthetic raw materials. Some Frutarom flavor products contain specialty fine ingredients made by the Company's Specialty Fine Ingredients activity exclusively for the Flavors activity.

8.9. Taste: Frutarom produces both sweet and savory flavors. The sweet flavors are used primarily for beverages, dairy products, ice creams, pastries and confections. The savory flavors are used primarily in the production of snacks, salty pastries, processed meat and fish, and convenience foods. Frutarom also produces unique seasoning mixes and functional ingredients for producers of processed meat, poultry and fish, as well as a variety of flavors for meat substitutes designed to help give a meaty flavor to products that do not contain any meat.

8.10. Form: Frutarom sells its flavor products in liquid, powder, emulsion, granulated, or paste form, sometimes blended with stabilizers and emulsifiers (ingredients which alter texture and other properties of the products to which they are added).

8.11. Composition: Frutarom produces both flavors which do not contain any fruit or vegetable matter or such, as well as a wide variety of food system products which do include, among other things, fruit, vegetable, and other natural components combined with flavorings. Food system products also include sweet and savory sauces such as pizza sauces and salad dressings, pre-made pasta fillings and other ready-made dishes plus other preparations based on sweet fruits for use in a wide range of food products such as dairy products (yogurts, ice cream, chilled desserts, butter and cheese), sweet and savory baked products, ready-to-eat meals and other convenience foods. Frutarom's capabilities in the food systems business enable it to combine a number of its fields of expertise since food systems usually combine flavors, natural flavor extracts, and natural functional food ingredients produced in the framework of its Specialty Fine Ingredients activity, enabling the Company to offer its customers comprehensive solutions tailored to their needs.

9. Breakdown of Revenues and Profitability

Following are figures reflecting the Company's revenues for 2012 through 2014 deriving from Flavors activity sales and their percentage of total Company revenues (in US$ thousands):

	2014	2013	2012
Total Company revenues	819,547	673,693	618,001
Revenues from Flavors activity	589,763	494,389	457,341
% of Total Company revenues	72.0%	73.4%	74.0%

Frutarom’s Flavors activity revenues rose 19.3% for the year to reach a record high of US$ 589.8 million, comprising 72.0% of overall Frutarom revenues, compared with US$ 494.4 million in 2013.

10. New Products

As part of its Flavors activity, Frutarom is constantly developing a variety of new products. New products are generally developed in collaboration with individual customers and adapted to their needs. None of the new products developed by the Company can be deemed material in terms of expected sales turnover and/or development costs.

11. Customers

11.1. The flavors manufactured by Frutarom are sold to an extensive customer base comprised of thousands of large multinational, medium-sized, local and small customers. The customers are mostly food and beverage manufacturers spread out in over 150 different countries worldwide.

11.2. The Flavors activity does not have any individual customer accounting for over 5% of Frutarom's sales turnover (over the past year there has also been no customer with purchases accounting for over 1.7% of Frutarom's sales turnover). Company management believes the Company is not dependent on any particular individual customer.

12. Competition

12.1. Frutarom's competitors in the flavors market are the multinational, medium-sized, and small local flavor manufacturers. Competition is largely based on the ability to be innovative, product quality, ability to provide value-added service to the customer, building and maintaining long-term relationships, reliability, and the development of products tailor-made to the customer's needs and aligned with future market directions. As the cost of flavors constitutes a negligible part in the overall cost of the end product, flavor market customers tend to be less sensitive to price when choosing their supplier. Flavor manufacturers must differentiate themselves by building close relationships with their customers, gaining familiarity and a thorough understanding of target markets, maintaining top-level R&D capabilities and capacity for innovation, and establishing a reputation for giving customers consistent, reliable and efficient service.

12.2. For further information regarding manufacturers operating in the flavor and fragrance market and Frutarom's position among them, see section 6.3 above. For information on factors influencing the Company's market position in the flavors industry, see section 7.20 above ("key success factors in the flavors field").

Specialty Fine Ingredients Market

13. ***Overview of the Specialty Fine Ingredients Market***

General

13.1. The specialty fine ingredients market in which the Company operates produces a wide range of products for a variety of industries. Frutarom's Specialty Fine Ingredients activity is focused mainly on developing, producing and marketing natural fine ingredients for the food and beverage, flavor and fragrance, pharma/nutraceutical, cosmetic and personal care industries. Fine ingredients are often sold directly to food and beverage manufacturers who use them in producing consumer products. Flavor and fragrance manufacturers use fine ingredients products as a foundation in producing their flavor and fragrance substances.

13.2. Frutarom operates in areas of the specialty fine ingredients market that include natural flavor extracts, natural functional food ingredients, natural pharma/nutraceutical extracts, specialty essential oils, algae, natural colors, natural antioxidants used in providing food protection solutions, citrus products, aromatic chemicals, and natural gums and resins.

13.3. According to estimates by Markets and Markets,[14] sales of specialty fine ingredients to food and beverage industries around the world (including sales of flavors and other ingredients) are expected to grow at an annual rate of 5.81% during the period of 2012 – 2018.

Characteristics of the Fine Ingredients Market

13.4. Research and development: Innovation is a key to success in the specialty fine ingredients market. R&D for new specialty fine ingredients products is a complex process requiring high levels of expertise, experience and investment. Developing a new ingredient often takes longer than developing a flavor product. Natural specialty fine ingredients are sometimes tailor-made to a customer's needs and require a long-term relationship with the customer and collaborative efforts in the product's development.

13.5. Production: The production of specialty fine ingredients tends to be more sophisticated and complicated than the production of flavors, requiring extensive knowhow. In addition, the production of specialty fine ingredients requires a large capital investment for building manufacturing facilities as well as for expanding production capacity when necessary. Production of specialty fine ingredients must also comply with stricter environmental and regulatory standards.

[14] marketsandmarkets.com., April 2014

13.6. Supply chain: Customers constantly seek ways to optimize their levels of inventory so ingredient manufacturers must adhere to shorter lead times and maintain stocks locally in the main markets. Additionally, medium-sized and local customers purchase hundreds of ingredients in variably small quantities, whereas the large multinational makers of ingredients have strict policies concerning minimum order quantity and the use of standardized packaging while smaller manufacturers lack the sufficient operational flexibility and global supply chain needed to meet such needs. This creates a market opportunity for medium-sized fine ingredients producers.

13.7. High entry barriers: An established reputation and brand recognition, which take many years to develop, are key success factors for manufacturers in the specialty fine ingredients market. Customers require a high degree of reliability and consistency, considering that once an ingredient is incorporated into a food or beverage flavor they will rarely risk replacing the fine ingredients supplier in order to avoid impairing the quality of the flavor. A multinational fine ingredients manufacturer seeking to build up a competitive advantage also needs to comply with stringent regulatory, environmental, and inspection standards and demonstrate strong capabilities in research and development, production and its global supply chain, including capital investment in the construction of production facilities and the expansion of production capacity whenever necessary. These factors constitute substantial entry barriers.

13.8. Growing demand for natural products: The rise in consumer demand for natural products has brought about increased demand for a variety of natural fine ingredients such as natural flavor extracts and natural specialty essential oils for use in the end products. Natural fine ingredients tend to be more unique and less interchangeable, resulting in increasing customer loyalty. The lion's share of natural fine ingredients is tailor-made to customer needs. Frutarom focuses on developing natural products in addressing this global trend. For further details, see section 14.5 below.

13.9. Growing demand for natural functional food ingredients: Functional food is food with certain added ingredients which provide, or are perceived as providing, health benefits, such as juices or dairy products with health additives. Changing consumer preferences towards foods with health benefits are leading to a rise in demand for functional food. The dairy and beverage markets exhibit the highest growth in the use of natural functional; food ingredients. Many of the active ingredients used in functional foods are derived from plants and herbs under processes similar to those used in producing flavor extracts. Manufacturers of natural functional food ingredients are often required by food and beverage makers to provide a proven scientific basis, such as clinical studies, for the health benefits attributed to the ingredients.

13.10. Regulation, health, safety and certification: Fine ingredients used in both the food and beverage and pharmaceutical/nutraceutical industries are increasingly subject to strict health and safety standards and regulations. This trend is part of an overall trend of increased regulation in those industries. At the end of 2006 the European Commission came out with the REACH regulations for the registration, evaluation, authorization and restriction of all chemicals produced in or imported into the EU market. In December 2008 the EU adopted new regulations defining BAPs (Biologically Active Principles) and setting their labeling requirements and maximum quantities, which took effect on January 20, 2011. In January 2009 the EU adopted regulation 1334/2008 for food flavorings, setting the definition for natural products and how they should be labelled, which entered into effect on January 20, 2011.

Customers buying ingredients, especially specialty fine ingredients, require the manufacturers to provide certification that their products are in compliance with regulations and standards. Also, there is growing demand for products with certain proven qualities such as being GMO-free (free of any genetically modified organisms) or pesticide free (not containing any element sprayed with pesticides). Demand for Kosher and for Halal certified products is also increasing as the demographic base of consumers for such products expands. As a result, fine ingredients manufacturers need to document their production processes and adhere to strict standards. In addition, ingredients manufacturers are required to hold certification relating to various manufacturing standards such as ISO 22000, BRC (British Retail Consortium) Issue 7, IFS, SQS, and other standards for permissible labelling such as EU Food information for Consumers which sets rules for product labelling and for providing information on the subject of allergies, including on products that do not come packaged, and the Global Harmonized System (GHS).

Frutarom's specialty fine ingredients comply with strict health, safety, and quality standards. For further details, see section 14.4 below.

13.11. Sourcing: Long term relationships with suppliers, growers and/or producers are of fundamental importance for maintaining a high degree of product quality and ensuring the availability of raw materials used in the production of specialty fine ingredients. This is particularly true for natural raw materials which, being derived from agricultural crops, are seasonal in their supply.

13.12. High volume production of fine ingredients with low margins: Over recent years there has been an increase in production of many fine ingredients in certain countries such as China and India where the cost structure for manufacturers tends to be lower. Many such manufacturers are technically less sophisticated with limited R&D capabilities and focus more on large volume production with low profit margins. They also generally lack global marketing and sales platforms, brand recognition and approved supplier status. This has led certain fine ingredients' manufacturers to differentiate themselves from such low-cost manufacturers by developing close collaborative relationships with customers, providing higher added-value products and services, and investing in R&D with an aim to develop specialty fine ingredients products with higher margins.

Critical Success Factors in the Specialty Fine Ingredients Field

13.13. Company management believes that the critical success factors in the field of Specialty Fine Ingredients are:

- Positioning and reputation as a reliable supplier – It is critical for suppliers to establish a solid reputation in the market, to develop and maintain strong ties with their customers and provide reliable service;

- Research and development, innovation and a supply of new and unique products – See section 13.4 above;

- Compliance with regulatory, quality and safety standards – See section 13.10 above;

- Raw material procurement – It is becoming increasingly important to direct resources towards focused procurement from countries that are major sources for numerous natural raw materials used in producing specialty fine ingredients, such as China, India and Brazil, while expanding the pool of suppliers and capitalizing to the fullest extent on cost reduction opportunities through global sourcing and strengthening ties with manufacturers, processers and growers of raw materials, particularly natural raw materials, in order to ensure their continuous and reliable supply over time and improve purchasing costs. Sourcing quality raw materials and timing their purchase correctly is the key to keeping up with short lead times to customers and requests for varying quantities and levels of quality;

- Wide geographic deployment for supporting multinational customers – The wide geographic spread of the support systems that provide the Company's multinational customers with assistance throughout their operating hours in their own language and location is of critical importance.

14. ***Products, Services and Added-Value Provided from Fine Ingredients Activity***

14.1. Under its Specialty Fine Ingredients activity Frutarom develops, manufactures, markets and sells natural flavor extracts, natural functional food ingredients, natural pharma/nutraceutical extracts, algae, natural antioxidants used in providing food protection solutions, specialty essential oils, citrus products, aroma chemicals, natural gums and resins, natural colors, and other products as well.

14.2. Sales of Specialty Fine Ingredients jumped from US$ 49 million in 2000 to US$ 158.4 million in 2014. The rise in Specialty Fine Ingredients sales in mainly due to the developing of new innovative products, focusing on both multinational and medium-sized locally-based customers, and strategic acquisitions that were successfully executed. Specialty Fine Ingredients accounted for a 19% share of Frutarom's total sales in 2014. Its products are sold mainly to the food and beverage, flavor and fragrance, pharmal/nutraceutical, cosmetics and personal care industries. Frutarom is working towards expanding the portfolio of products offered to its customers in the fields of food, health, and cosmetics while entering and expanding its activity in other growing fields including natural colors, natural food protection solutions, and natural protection solutions for livestock feed and for pet foods.

14.3. Frutarom has an established reputation in the market for fine ingredients and a broad customer base of both multinational and locally-based medium-sized customers which are supported by Frutarom's sales and marketing team and the Company's efficient global supply chain. Frutarom has warehouses located in Europe, the USA, Central and South America, Asia and Africa, allowing it to supply customers quickly – usually within days. Although most of the fine ingredients made by Frutarom are sold to external customers (including competing flavor manufacturers) some is consumed internally and certain types, such as in the citrus and natural health fields, are used exclusively by Frutarom in developing and producing unique taste and health solutions, giving Frutarom a competitive edge.

14.4. Frutarom's specialty fine ingredients meet strict health, safety and quality standards such as ISO 22000, FSSC 22000, Swiss GMP, British BRC and ISO 9000. Most of Frutarom's fine ingredients are also GMO-free and pesticide-free as well as being Kosher and/or meeting Halal requirements.

14.5. Frutarom focuses on the development of natural products in response to the growing trend globally towards consumption of natural products, considered to be healthier. Frutarom management believes the Company is one of the world leaders in this field and successfully combines its experience and reputation of over 80 years of research, development, production, and marketing of natural specialty fine ingredients with its ability to offer a wide variety of products based on an efficient global supply chain. Frutarom’s in-depth knowledge of the flavors market and food industry customers' requirements as well as the specialty fine ingredients market allows it to be positioned at a unique junction for delivering solutions that combine taste and health.

14.6. Frutarom believes that its relationship with and close familiarity with the foods and beverages market give it a competitive advantage in the functional foods market. This advantage is backed up by its R&D capabilities, proprietary production methods, and experience in conducting clinical studies.

As mentioned above, Frutarom’s Specialty Fine Ingredients activity is divided into several main categories:

14.7. **Natural Flavor Extracts**: Frutarom is a leading manufacturer of a wide variety of natural flavor extracts produced from fruits, plants and other botanical material. The main customers for natural flavor extracts produced by the Company are food and beverage manufacturers, flavor and fragrance companies (including the Company's own Flavors activity) and, to a lesser extent, tobacco companies. The natural flavor extracts are generally products tailor-made to customer specifications and the Company works in close collaboration with its customers in developing and manufacturing the desired flavor extract.

14.8. **Natural Functional Food Ingredients**: The Company offers a variety of natural extracts used as raw materials in the manufacture of functional food ingredients. Functional foods are foods such as breakfast cereals, health drinks and yogurts which contain specialty fine ingredients that provide them with healthy properties. Natural functional food ingredients require various certifications but are subject to fewer restrictions than herbal extracts. The main customers for the natural functional food ingredients are in the food and beverage industry.

14.9. **Natural Pharma/Nutraceutical Extracts**: Frutarom manufactures a wide variety of natural herbal extracts with certain medicinal and health benefits used in the manufacture of prescription drugs, non-prescription medications, and natural dietary supplements. The main customers for natural herbal extracts are pharmaceutical and nutraceutical companies and the makers of food supplements.

14.10. **Specialty Essential Oils and Citrus Products**: Frutarom produces a wide range of specialty essential oils and is a leading producer of specialty citrus products. Specialty essential oils produced by Frutarom include those derived from citrus (such as orange, grapefruit, lemon and mandarin), mints, flowers, spices, herbs and from trees. These products are used in food and beverage, flavor and fragrance, pharmaceutical, and cosmetic and other personal care products.

Company management considers Frutarom to be a global leader in the field of specialty citrus products used in creating citrus flavoring in foods, beverages, perfumes and other personal care products. Frutarom has been active in the field of specialty citrus extracts since 1933. Frutarom continuously invests in unique innovative technologies for the processing, extraction and distillation of specialty citrus products. In February 2014 Frutarom acquired the activity of CitraSource, specializing in the research and development, production, marketing and sales of specialty solutions in the field of citrus Its state-of-the-art plant in Florida and global purchase capabilities in this field which strengthen Frutarom's position as a leading player in the development, production and sales of specialty citrus products. A number of Frutarom's specialty citrus products are reserved for the exclusive use of the Flavors activity and are not sold to other parties, thereby giving the Company a competitive advantage in the production of citrus flavors. For further details on the acquisition of CitraSource, see the Company’s immediate report dated February 25, 2014.

14.11. **Algae**: In recent years Frutarom, together with Israel's Ben Gurion University, has invested in the field of algae, considered worldwide to be very attractive as a dietary supplement (a source of Omega 3), medicinal agent, and as an element in various cosmetic products. The specialty algae is grown for productions purposes on a farm in the south of Israel. Frutarom extracts the active substance from the algae using natural processes and markets these to food, dietary supplement, cosmetics and personal care companies throughout the world.

14.12. **Natural Solutions for Food Protection**: in recent months Frutarom has expanded its activity in the field of natural food protection which ensures the protection of the consumer's health and the extension of the product's shelf life. This line of solutions includes antibacterial components and antioxidant substances – all based on natural substances. Frutarom recently made two acquisitions in this field – Vitiva in Slovenia and Ingrenat in Spain – which will contribute towards the continued development of this growing and important area of activity.

14.13. **Natural Colors**: Frutarom utilizes its R&D, production, and marketing infrastructures in the field of food and beverages to develop natural color solutions based on natural extracts from vegetables, fruits, and other natural substances. Frutarom recently carried out two important acquisitions in this field – Montana Food and Vitiva – which will help it significantly expand its activity in this important and growing field over the coming years. Natural colors can be sold to food and beverage customers as part of taste solutions or on a standalone basis. Natural colors are also sold to the cosmetic and pharma industries.

14.14. **Aroma chemicals**: Frutarom produces about 700 types of aroma chemicals which are used in the manufacture of flavors and fragrances, foods, animal feed, cosmetics, oral hygiene products and other products. Frutarom is a leading global player in the field of unique aroma chemicals, focusing on R&D, manufacturing and selling of high-added-value specialty aroma chemicals, and continuously changing its product mix in this area towards low volume, high margin products. The variety of aroma chemicals produced by Frutarom range for use by the flavor and fragrance industry includes diketones and pyrazines used for creating aromas of roasting and toasting. Frutarom also produces unsaturated aldehydes which impart a cool freshening sensation when used orally or applied to the skin and are used, among other things, in the manufacture of candies, chewing gum, skin care products and oral hygiene products.

14.15. **Natural Gums and Resins**: Frutarom offers a range of natural water soluble gums and resins derived from a variety of botanical sources including certain types of gum trees as well as seeds, seaweed and beet sugar. The natural water soluble gums and resins are used in the production of foods, beverages, pharmaceuticals and cosmetics and are sold mainly to food, beverage and flavors manufacturers and pharmaceutical companies.

15. Breakdown of Revenues and Profitability

Following are figures reflecting the Company's revenues for 2012 through 2014 (in US$ thousands) deriving from Specialty Fine Ingredients activity and their percentage of total Company revenues:

	2014	**2013**	**2012**
Total Company revenues	819,547	673,693	618,001
Revenues from Specialty Fine Ingredients activity	158,375	145,591	140,763
% of Total Company revenues	19.3%	21.6%	22.8%

16. New Products

Frutarom develops new Specialty Fine Ingredients as part of its ongoing activity in order to continue strengthening its position and improve its product mix, including the replacement of low margin products with new innovative and unique products with higher profit margins. None of the new products developed by the Company can be deemed material in terms of expected sales turnover and/or development costs.

17. Customers

17.1. The specialty fine ingredients manufactured by Frutarom are sold to an extensive customer base comprised of a vast number of large multinational, medium-sized, local and small customers in the food and beverage, pharma/nutraceutical, flavors and fragrance, and personal care industries.

17.2. The Specialty Fine Ingredients activity does not have any individual customer accounting for over 5% of Frutarom's sales turnover (in recent years there has also been no customer with purchases accounting for over 1.9% of Frutarom's sales turnover). Company management believes the Company is not dependent on any particular individual customer.

18. Competition

18.1. Competition In the specialty fine ingredients market varies by product category.

18.2. In natural flavor extracts the Company's competitors are manufacturers specializing in the production of natural flavor extracts, such as Naturex, pharma/nutraceutical manufacturers, and multinational and medium-sized producers of flavors and fragrances that manufacture specialty fine ingredients mainly for their own use, such as Givaudan, IFF, Symrise, Sensient, Robertet and Mane.

18.3. In the natural functional food ingredients and the pharma/nutraceutical categories, Frutarom's competitors are mainly pharma/nutraceutical companies specializing in this area, such as Indena S.p.A., Naturex, and Martin Bauer GmbH & Co. and KG, as well as small start-up companies that specialize in unique and innovative products and technologies.

18.4. Frutarom's competitors in the essential oils field include companies such as Treatt PLC which focus on the manufacture of essential oils including specialty essential oils, and large and medium-sized multinational flavor manufacturers that produce specialty essential oils primarily for their own use. There are also growers and processors of essential oils, mainly in developing countries, represented by traders and distributors of specialty essential oils also competing in the essential oils market.

18.5. In aroma chemicals the Company competes with large multinational flavor & fragrance manufacturers that produce specialty aroma chemicals for their own use and sale into the market. Other competitors in this field are highly specialized manufacturers in the production of aroma chemicals based in Europe and USA. Other manufacturers of aroma chemicals are generally low cost producers, mostly located in Asia, with limited direct sales and marketing platforms and often reliant on dealers for marketing and selling their products. There are also chemical companies that produce aroma chemicals in high volumes as part of their wider product offering, but in most cases they do not produce specialty aroma chemicals. Frutarom, for the most part, does not compete with these, but focuses rather on low-volume specialty aroma chemicals with relatively higher margins due to the unique manufacturing facilities required in their production.

18.6. For further information regarding manufacturers operating in the specialty fine ingredients market, see section 6.3 above. For details on factors affecting the Group's position in the specialty fine ingredients market, see section 13.13 above ("Critical success factors in the specialty fine ingredients field").

19. Production Capacity

For information on the Company's production capacity for specialty fine ingredients, see section 23 of this report.

20. Frutarom's Trade and Marketing Activity

20.1. As stated above, in addition to its core activities Frutarom also engages in the importing and marketing of various raw materials that it doesn't produce itself for the food, pharmaceutical, chemicals, cosmetic, and detergent industries as part of its service and the furnishing of comprehensive solutions to its customers to help strengthen its ties and promote sales of its core products while maintaining long lasting and closer relations with the customers.

20.2. The raw materials sold and marketed by Frutarom under its Trade and Marketing activity are mainly raw materials that the Company purchases for the manufacture of its specialty fine ingredients and flavors. As Frutarom imports and purchases these materials in bulk or in large quantities, it can buy them at attractive prices and sell them at a premium to third parties. The Trade and Marketing activity is synergetic with and supports Frutarom's core activities – Flavors and Specialty Fine Ingredients – through the leveraging of its sales structure, supply chain, procurement, and global management, enabling it to offer a wider variety of products and solutions and to add value to its customers, especially medium-sized and locally-based customers in emerging markets, and deepening the cooperation with these customers.

20.3. Frutarom does not consider the Trade and Marketing activity part of its core activities. In 2014 this activity totaled US$ 78.5 million. Most of the growth in this activity in recent years was due to the acquisition of Etol, PTI and Montana Food and it is concentrated in Eastern Europe, Latin America and Israel. In view of the fact that this activity is not material to Frutarom, it is not covered separately in this report.

CHAPTER 4 – DESCRIPTION OF THE COMPANY'S BUSINESS:

MATTERS CONCERNING THE COMPANY'S OVERALL ACTIVITY

21. Marketing and Distribution

21.1. Frutarom maintains a global marketing, sales and customer technical support structure which is based on local R&D, sales and marketing personnel in its main target markets. The Company believes its global presence gives it a competitive edge and is a key part of its growth strategy. As of December 31, 2014 Frutarom had 1,174 people working in sales, marketing and R&D, 73 sales and marketing offices, and 42 R&D labs located in its main target markets in close proximity to its customers, including in the US, the UK, Germany, Switzerland, France, Italy, Slovenia, Norway, Denmark, Belgium, Holland, Poland, Macedonia, Czech Republic, Romania, Serbia, Turkey, Russia, Ukraine, Kazakhstan, Slovakia, Israel, Mexico, Brazil, Costa Rica, Guatemala, Peru, Chile, China, Vietnam, Japan, Hong Kong, Indonesia, India, Nigeria and South Africa. The Company markets and sells its products primarily through its own sales personnel. In some countries Frutarom retains third party agents and distributors to sell its products.

21.2. Frutarom's global sales and marketing organization is a key component of its strategy to supply products tailor-made to its customers' needs, along with specialized products and services and high quality customer support to both large multinational and medium-sized locally-based customers.

21.3. Frutarom differentiates itself from its competitors by, among others things, offering its medium-sized and local customers the same level and quality of service and customization of products to customer needs as it provides to large multinationals. Frutarom's sales and marketing staff and R&D personnel work closely with both large multinational and medium-sized and local customers to offer the same timely and accessible individualized development services, including the development of custom flavors and specialty fine ingredients tailor-made to their specific needs. The Company estimates that the market segment of medium-sized and locally-based customers whose sales turnover is less than US$ 1 billion represents over 60% of the global food and beverage market.

21.4. The Flavor and Specialty Fine Ingredients activities each have their own separate sales, marketing and customer support teams. However, Frutarom assigns a dedicated salesperson to any customer purchasing the products of both activities, enabling the Company to better respond to the customers' needs and to identify and capitalize on opportunities for selling the wide range of its products to the same customer. See the graph in section 2.5 above (Customer in the Center).

21.5. The Flavors activity's sales, marketing and customer support activities focus primarily on customers in the food and beverage industries, while those of the Specialty Fine Ingredients activity focus also on customers in the flavor and fragrance, pharma/nutraceutical and personal care industries.

21.6. Frutarom's sales and marketing team constitutes an important link between the Group's customers and its R&D team. Work is done in close collaboration with customers in order to understand their particular needs while relaying the information and fully cooperating with the R&D team which develops the products custom-made to the customer's specific needs, in some instances in close cooperation with the customer's development staff.

21.7. In certain cases, particularly in emerging markets, Frutarom offers its customers technological and marketing support in order to help them expand and improve their product offering and quality and their manufacturing processes. Frutarom believes this approach strengthens its relationships with these customers and helps boost demand for its products.

21.8. Company management believes that Frutarom is not dependent on any of its marketing channels.

22. <u>Seasonality</u>

22.1. The Company’s activity in recent years has been affected by seasonal fluctuations which were reflected, until the acquisition of PTI, by sales and profitability being weaker in the first and fourth quarters (the fourth quarter being the weakest of the year) and stronger in the second quarter. Following the acquisition of PTI, where seasonality in recent years has been expressed by the fourth quarter being the strongest and the first quarter the weakest in terms of sales turnover as well as in terms of profits and profitability, there has been a certain change in Frutarom's seasonality profile.

22.2. Following is the quarterly profit and loss reports for 2013-2014 (in $US millions):

	Q4 2014	Q3 2014	Q2 2014	Q1 2014	Q4 2013	Q3 2013	Q2 2013	Q1 2013
Sales	202.2	210.8	218.1	188.5	191.8	161.0	168.6	152.2
Gross Profit	79.6	81.6	85.9	73.5	70.2	62.6	66.9	57.2
Selling, marketing, R&D, G&A and other expenses	50.8	50.6	50.6	49.6	49.9	40.0	41.9	38.3
Income from Operations*	28.7	30.9	35.3	23.9	20.3	22.6	24.9	18.9
EBITDA*	36.5	39.0	43.4	32.1	28.3	29.4	32.5	25.8
Financial expenses **	5.6	0.8	2.3	1.5	2.5	1.3	2.3	1.4
Income before taxes	23.1	30.2	33.1	22.5	17.8	21.3	22.6	17.5
Net income	19.7	24.2	25.5	18.3	15.0	17.0	17.6	14.0

* Non-recurring expenses amounting to approximately US$ 5.1 million affected income from operations in 2013 (reorganization expenses of US$ 2.5 million, and adjustments and acquisition expenses of US$ 2.6 million). Figures for 2014 include non-recurring expenses totaling approximately US$ 1.1 million, mainly attributable to acquisitions.

** Financial expenses included non-recurring expenses totaling US$ 4.5 million for revaluation of financial liabilities pertaining to option to purchase Vantodio's remaining shares due to PTI producing better results than were expected.

.

23. *Fixed Assets, Land, Facilities and Production Capacity*

As of the date of publication of this report, Frutarom operates 37 production sites throughout the world. The following table outlines Frutarom's main production sites and the activity performed there:

Country	Location	Field of activity	Property size (m^2)	Buildings – Ownership/ Lease/Rent	Land - Ownership/ Lease/Rent
Israel	Haifa [15] [16]	Flavors and fine ingredients	35,490	Ownership	Lease
Israel	Acre [15]	Flavors	9,273	Ownership	Lease
Switzerland	Wädenswil	Fine ingredients	13,464	Ownership	Ownership
Switzerland	Reinach	Flavors	43,000	Ownership	Ownership
Germany	Emmerich	Flavors	19,000	Ownership	Ownership
Germany	Sittensen	Flavors	10,001	Ownership	Ownership
Germany	Stuttgart (Gewürzmüller) [17]	Flavors	13,600	Lease	Rent
UK	Hartlepool	Fine ingredients	31,971	Ownership	Ownership
UK	Wellingborough	Flavors	8,090	Ownership	Ownership
USA	North Bergen (NJ)	Fine ingredients	32,000	Ownership	Ownership
USA	Corona (CA) [18]	Flavors	14,000	Rent	Rent

[15] Frutarom Ltd. possesses rights to land located in the Acre industrial zone and in the Haifa Bay section of Haifa. The net discounted value of the leasing fees for the land amounts to approx.US$ 1,077,000 as of December 31, 2014 (approx. US$ 1,109,000 as of December 31, 2013). The land leasing rights are for 49 year periods ending 2032 -2042. Frutarom Ltd. has the right to extend the leasing for an additional 49 year period. The land on which the Company's plant in Haifa is located is subject to long-term lease agreements with the Israel Land Authority (excluding that stated in footnote 13 below). The net discounted value of the leasing fees appears in the financial statements under property, plant and equipment.

[16] The total size of the Haifa site is 35.5 dunams and includes within it a 7.3 dunam area rented from a third party under an operating lease ending February 28, 2015, with an option to extend it until August 31, 2016. The annual rental fee for 2013 was NIS 990,000. The annual rental fee for 2014 was NIS 1,008,000.

[17] The land and buildings of the Company's plants in Stuttgart are rented by the Company from a third party under a rental agreement for a period of 10 years ending October 1, 2017. The annual rental fee is € 600,000 a year (€ 544,000 for the Gewürzmüller plant and EUR 56,000 for the Blessing plant). According to the agreement, the Company has a unilateral option [for] a 5 year extension. If the option is exercised, rental fees will be updated in line with prevailing market rates for similar assets at that time and adjusted for changes in the German consumer price index. At the end of the rental period, the agreement will be automatically extended by additional periods of two years each until either side serves notice for terminating the agreement at least one year in advance. The Company is entitled to terminate the rental agreement by giving advance notice of one year.

Country	Location	Field of activity	Property size (m^2)	Buildings – Ownership/ Lease/Rent	Land - Ownership/ Lease/Rent
USA	Cincinnati (Ohio)	Flavors	57,000	Ownership	Ownership
China	Kunshan [19]	Flavors	15,000	Ownership	Lease
China	Qing Pu, Shanghai[20]	Fine ingredients	14,500	Ownership	Ownership
Italy	Parma	Flavors	7,500	Ownership	Ownership
Slovenia	Škofja Vas (Etol)	Flavors	65,000	Ownership	Ownership
Slovenia	Markovci - Vitiva	Fine ingredients	42,000	Ownership	Ownership
Brazil	Porto Feliz, State of Sao Paulo	Flavors	8,000	Ownership	Ownership
Guatemala	Guatemala City	Flavors	1,022	Ownership	Ownership
Russia	Moscow (Platinum Absolut)	Flavors	12,000	Rent	Rent
Russia	Moscow - TSP	Flavors	6,100	Ownership	Ownership
Peru	Lima	Flavors	19,645	Rent	Rent
Spain	Murcia	Flavors	44,032	Ownership	Ownership

The facilities and properties owned by the Group are presented in the financial statements under the Group's property, plant and equipment within the line item for land and buildings. All of the Group's rental agreements are defined as operational rent and therefore are not included and presented as assets.

The Company also has production facilities which are not significant in terms of the Company's scope of activity.

[18] The land and buildings of the Company's plants in Corona are rented by the Company from a third party until February 28, 2025 at an annual rental fee of US$ 403,600 increases by another 3% each year.

[19] The subsidiary company in China has land usage rights of for a 50-year period ending in 2046 The net discounted value of the leasing fees for the land is approx. US$ 159,000 as of December 31, 2014 (US$ 167,000 as of December 31, 2013). The net discounted value of the leasing fees appears in the financial statements under property, plant and equipment.

[20] The consolidated company in China has land usage rights for a period of 60 years ending in 2063. Net discounted leasing fees for the land are approx. US$ 1,264,000 as of December 31, 2014 (approx. US$ 1,264,000 as of December 31, 2013) The discounted leasing fees are presented in the financial statements under property, plant and equipment.

Following is a description of the Company's significant plants:

- **Haifa, Israel** – At its plant in Haifa the Company produces flavors and specialty fine ingredients (specialty essential oils, specialty citrus products and aromatic chemicals) in the framework of its two activities. The plant also contains management offices.

  Production capacity and shifts – Flavor production is carried out five days a week on one shift. The plant has additional potential production capacity of approximately 100% if it were to employ three shifts. Production of fine ingredients at the plant takes place five days a week using three shifts.

- **Acre, Israel** – At its plant in Acre the Company produces flavor mixes (mainly savory flavors).

  Production capacity and shifts – The plant operates five days a week using one shift. It has additional potential production capacity of approximately 100% if it were to employ three shifts.

- **Wädenswil, Switzerland** – The Company produces natural extracts at the plant in Wädenswil for its Specialty Fine Ingredients activity.

  Production capacity and shifts – The plant operates five days a week in two shifts. It has additional potential production capacity of about 30%-40% if it were to run three shifts.

- **Reinach, Switzerland** – The Reinach plant is used by the Company to produce mainly food systems as part of the Flavors activity.

  Production capacity and shifts – The plant runs five days a week with about two shifts a day and would potentially gain about 20%-25% in output capacity were it to switch to running non-stop with three shifts.

- **Emmerich, Germany** – The Emmerich plant is used by the Company to produce mainly food systems as part of the Flavors activity.

  Production capacity and shifts – The plant operates five days a week with about two shifts a day. It has additional potential production capacity of about 25%-30% if it switched to running non-stop with three shifts.

- **Sittensen, Germany** – The Company produces savory flavor mixes and seasonings at this plant in the framework of its Flavors activity.

  Production Capacity and shifts – The plant works five days a week in two shifts. It has 25%- 30% in additional potential production capacity were it to switch to running non-stop with three shifts.

- **Korntal, near Stuttgart, Germany (Gewürzmüller)** – The Company produces savory flavor mixes and seasonings at the Stuttgart plant as part of its Flavors activity.

  Production capacity and shifts – The plant operates five days a week with one shift. It has additional potential production capacity of approximately 100% if it were to switch to non-stop production employing three shifts.

- **Wellingborough, UK** – The Company makes flavors at this plant.

  Production capacity and shifts – The plant works five days a week with one shift for flavors production. The plant has additional potential production capacity of 100% if run using multiple shifts.

- **Hartlepool, UK (Oxford)** – Aromatic chemicals are produced by the Company at this plant under its Specialty Fine Ingredients activity.

  Production capacity and shifts – The plant operates five days a week in three shifts. It has additional potential production capacity of about 25% assuming continuous production 7 days a week.

- **North Bergen (NJ), USA** – At this plant Frutarom produces natural extracts from plants, gums and resins in the framework of its Specialty Fine Ingredients activity.

  Production capacity and shifts – The plant works five days a week with two shifts in some of the production departments. The plant has additional potential production capacity of about 35% if it switched to continuous production 7 days a week with three shifts.

- **Corona (CA), USA (FSI site)** – The Company's plant in Corona (California) manufactures flavor extracts for its Flavors activity.

  Production capacity and shifts – The plant runs 5 days a week most of the year and uses $1^1/_2$ to 2 shifts during the summer. It has additional potential production capacity of approximately 60%-70% were it to switch to continuous production using three shifts.

- **Cincinnati, USA (Flavor Systems site)** – The Company's plant in Cincinnati, Ohio produces flavors.

  Production capacity and shifts – The plant runs 5 days a week on one shift most of the year and $1^1/_2$ to 2 shifts during the summer. It has potential of approximately 60%-70% more output capacity were it to switch to non-stop production with three shifts.

- **Kunshan, China** – Flavors are produced at this plant under the Company's Flavors activity.

  Production capacity and shifts – The plant operates five days a week on one shift. It can potentially increase production capacity by approximately 100% by running multiple shifts.

- **Qing Pu, Shanghai, China** – The Company will produce Flavors and Specialty Fine Ingredients at this plant starting in the second quarter of 2015.

  Production capacity and shifts – The plant operates five days a week on one shift. It can potentially increase production capacity by approximately 200% by running multiple shifts.

- **Parma, Italy** – The plant in Parma produces savory flavor mixes in the framework of the Company’s Flavors activity.

  Production capacity and shifts – The plant works 5 days a week with one shift and could potentially raise its production capacity by about 100% if it changed to continuous production of three shifts.

- **Škofja Vas, Slovenia** – At its plant in Škofja Vas the Company produces mostly flavors, beverage bases, food systems and savory flavor mixes under its Flavors activity.

  Production capacity and shifts – The plant works 5 days a week on $1^{1}/_{2}$ shifts and could potentially boost output capacity about 40%-50%.

- **Markovci, Slovenia (Vitiva)** – At this plant the Company Frutarom produces antioxidants, natural colors, natural sweeteners, plant extracts for functional foods, and food and pharma additives under its Flavors activity.

  Production capacity and shifts – The plant works 7 days a week on 3 to 4 shifts. The plant exhausts its full potential production capacity.

- **Porto Feliz (Sao Paulo), Brazil** – The plant produces extracts as part of the Company's Flavors activity.

  Production capacity and shifts – The plant works 5 days a week on one shift and would potentially gain about 100% in output capacity for flavors if it switched to continuous production using three shifts.

- **Guatemala City, Guatemala (Aroma site)** – At this plant Frutarom manufactures flavors (mostly sweet) for beverages, dairy products, sweets, snacks and other food items as part of its Flavors activity.

  Production capacity and shifts – The plant is run $5^{1}/_{2}$ days a week on one shift. It has additional potential production capacity of about 100% were it to be run on three shifts.

- **Moscow, Russia (PTI – Platinum Absolut site)** – Here Frutarom manufactures spice mixes and functional ingredients for the food industry as part of its Flavors activity.

  Production capacity and shifts – The plant works five days a week with one shift. It would have about 100% more potential production capacity if it went over to continuous production of three shifts.

- **Moscow, Russia (PTI – TSP)** – At this plant, as part of its Flavors activity, Frutarom manufactures protein-based specialty fine ingredients using advanced technology with special emphasis on processed meats and convenience foods.

  Production capacity and shifts – The plant runs five days a week on 2 or 3 shifts, according to need. It could potentially increase production capacity by about 50% were it to run 7 days a week.

- **Lima, Peru (Montana Food)** – At this plant Frutarom manufactures flavors and natural food colors as part of its Flavors activity.

  Production capacity and shifts – The plant runs five days a week on 1 to 2 shifts and could potentially increase production capacity by about 50%.

- **Murcia, Spain (Ingrenat)** – At this plant Frutarom manufactures natural plant extracts in the framework of its Specialty Fine Ingredients activity.

  Production capacity and shifts – The plant runs five days a week on 2 shifts for 8 months a year. It could potentially increase production by about 100% were it to switch to 2 shifts year round.

24. Research and Development

24.1. Frutarom considers its research and development system one of its key core proficiencies and channels substantial resources towards researching and developing new innovative products. As of December 31, 2014 the Company's workforce included 411 employees engaged in R&D. Frutarom has over 80 years of experience in research and development in the field of flavors and specialty fine ingredients, with particular attention given to natural flavors and specialty fine ingredients. Frutarom's R&D is crucial to its future success as most of its products, and natural products in particular, are tailor-made and customized in accordance with its customers' needs. As part of its R&D activities and in order to broaden its lineup of natural, innovative and unique products, Frutarom strives to create cooperative ties with academic institutions, research institutes, and start-up companies in Israel and throughout the world. Frutarom has created a number of such bonds which serve to beef up and strengthen its pipeline of new innovative products that it intends to launch in the coming years.

24.2. In many cases the development of fine ingredients is initiated by the Company after analyzing market trends and needs, while focusing on the development of products with higher profit margins in order to continue improving the product mix and ensure that its production capabilities and capacity are put to optimal use.

24.3. The development of new or customized flavor products is a complex process that calls for the combined knowledge and expertise of the Company's scientists and flavorists. Scientists from various disciplines work in project teams that include flavorists to develop new flavors whose qualities reflect consumer preferences. The development of new flavor compounds is as much an art as it is a science, requiring an in-depth understanding of the characteristics and features of the flavor and of the various ingredients used in creating it. To a large extent the process of developing a new flavor involves trial and error.

24.4. As of the date this report is being published, Frutarom's Flavors activity has 34 R&D laboratories, with the main ones located in the United Kingdom, Switzerland, Germany, the United States, Slovenia, Israel, Russia, Peru, Italy, France, Turkey, China, Brazil and South Africa. For its Fine Ingredients activity, Frutarom has 13 R&D facilities located in Israel, the UK, Switzerland, the United States, Peru, Slovenia, Spain, China and the Netherlands.

24.5. The Company recognized all research and development costs in its books as current expenses when incurred. For more information see Note 2(f)(6) and Note 20(b) to the financial statements.

24.6. For further information concerning liabilities recognized in the financial statements for grants received and amounts recognized as research and development expenses, see Note 2(f)(6) and Note 11(a)(2) to the financial statements.

25. <u>Intangible Assets</u>

25.1. Frutarom’s intellectual property mainly includes the formulas used in creating its flavors and the development and production processes for fine ingredients. Frutarom does not register its formulas as patents, but nevertheless they are highly confidential and considered trade secrets that are restricted to a minimal number of people within the Group. Protecting formulas as trade secrets and not registering them as patents is common industry practice since patent registration would involve turning the formulas into public information, and the protection given to the manufacturer on them would end when the patent expires.

Nonetheless, the Company does have registered patents which mainly concern production processes for ingredients developed by the Group and for products in the pharma/nutraceutical field. The Company also registers trademarks on some of its products in some of the countries in which it operates. To protect its intellectual property, the Company includes confidentiality, non-competition, and transfer of intellectual property rights clauses in its personal employment contracts with employees, contracts with consultants, and in agreements with suppliers and customers. Frutarom believes itself not materially dependent on any single intellectual property right, product formula, patent or license.

25.2. Not in all countries where the Group operates has the "Frutarom" trademark been registered. There are countries with registered trademarks similar to the name "Frutarom" on goods similar to the Group's products. In the view of the Company's management, not having the "Frutarom" trademark registered in all countries in which it operates does not constitute a significant risk to the Group and its activities.

25.3. For details on amounts recognized as assets in the financial statements with regards to intangible assets, see Note 5 and Note 8 to the financial statements.

25.4. Intangible assets representing know-how and product formulas are amortized according to Group management's assessment of how long they can be useful since for most know-how and product formulas there is no technical or regulatory period of obsolescence, as well as in light of the Group's experience concerning its periods of use from the know-how and formulas in its possession and according to the industry in which the Group operates.

26. Human Resources

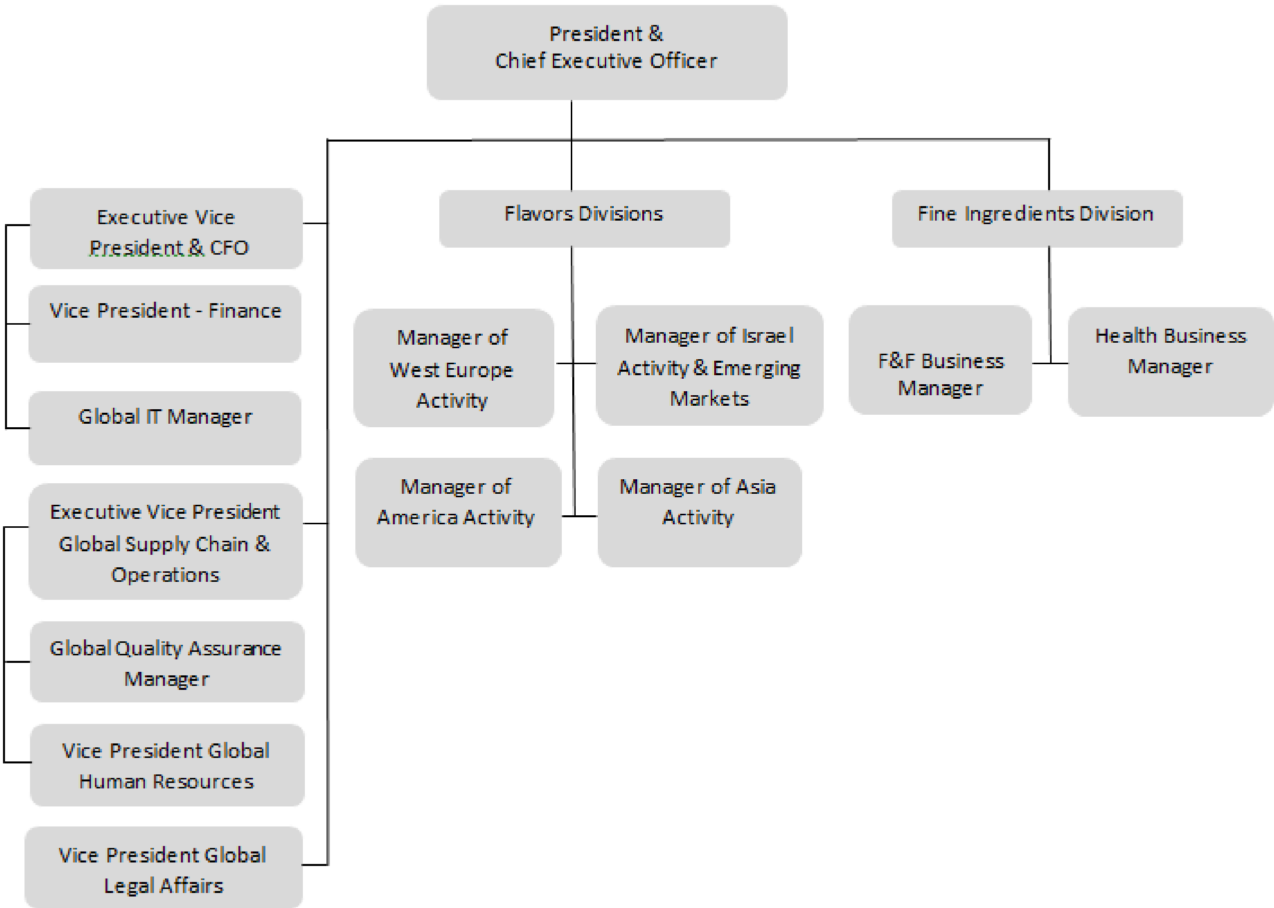
26.1. Frutarom had 3,034 employees as of December 31, 2014. The following table provides a breakdown of employees by country in the past two years:

Country	31.12.2014	31.12.2013
Israel	294	310
Switzerland	180	187
Germany	326	326
United Kingdom	304	298
United States	294	277
Belgium	36	34
China and the Far East	189	199
Russia	570	539
Ukraine	32	12
Kazakhstan	4	11
France	12	10
Turkey	26	26
Mexico	3	3
Brazil	82	74
Guatemala	56	55
South Africa	37	47
Italy	33	34
Norway	2	5
Czech Republic	3	3
Slovenia	217	224
Serbia	5	5
Slovakia	7	5
Macedonia	2	2
Poland	18	14
Peru	269	-
Chile	33	-
Total	**3,034**	**2,700**

26.2. The following table shows the breakdown of the Group's employees by field of activity in the past two years:

Field	31.12.2014	31.12.2013
Sales and marketing	763	678
R&D	411	365
Operations	1,406	1,251
Management	454	406
Total	**3,034**	**2,700**

26.3. Frutarom's organizational chart:



26.4. Most of Frutarom's workforce is employed based on personal employment agreements. These agreements vary from country to country according to the laws in force in each jurisdiction.

There are employees, mainly working at Company sites in Germany, Slovenia, USA, Israel (Haifa) and Italy who are covered by collective bargaining agreements. These agreements vary from country to country and deal principally with terms of employment, salaries, pension schemes, other benefits, hiring and dismissal of employees and procedures for settling labor disputes.

Directors and Senior Management of the Company

26.5. As of December 31, 2014 the Group's senior management includes five senior officers and its global management group includes around 10 additional members besides the members of senior management. The Company has personal employment contracts with members of management. As is customary in the industry in which the Company operates, these contracts include standard clauses covering non-competition, confidentiality, and transfer of intellectual property rights to the Company.

26.6. A number of members of the Company's senior management are entitled to extensions ranging between six and twelve months in their advance notice periods if their employment with the Company is terminated within a period of 12 months from the date when ICC Handels AG[21] holds less than 26% of the Company's share capital. In such a case, furthermore, some of the members of senior management are entitled to the immediate exercise of all options and/or ordinary shares granted to them in the past even if they have not yet been fully vested.

26.7. Company managers are covered by directors and officers liability insurance. The Company has also granted its senior officers an undertaking for indemnification in advance and exculpation for actions taken by virtue of their office in the Company, subject to the restrictions set out by law. For further details see regulation 22 in Chapter D ("Additional Information on the Corporation") of the Company's Annual Report for 2014.

26.8. On January 14, 2014 the General Meeting approved a compensation policy for the Company's senior officers after it was also approved by the Compensation Committee and the Company's Board of Directors. For details of the Compensation Policy, see the Company's immediate report on the matter dated December 29, 2013.

---

[21] To the best of the Company's knowledge, ICC Handels AG is a fully-owned subsidiary of ICC Industries Inc., Frutarom's principal shareholder.

27. Employee Incentive Plans

For details regarding the Company employee incentive plans, see Note 12(b) to the Company's financial statements.

28. Raw Materials and Suppliers

28.1. Frutarom purchases thousands of raw materials that go into its products from a very wide range of suppliers, having more than one supplier for most raw materials. The main raw materials purchased by Frutarom include plants, leaves and roots for producing natural flavor extracts, natural functional food ingredients and pharma/nutraceutical extracts. The Group also purchases essential oils for producing specialty essential oils such as citrus oils and mint oils. Other raw materials purchased by the Group include natural and synthetic chemicals, alcohol, esters, acids and oleoresins.

The Group's global and local supply chain managers and purchasing departments continually monitor raw material price trends, and action is taken to adjust the Group's selling prices accordingly when necessary. Frutarom is building a global purchasing unit to centrally support the purchase of raw materials classified as being strategically important.

28.2. No individual Frutarom supplier has supplied more than 10% of its raw material needs in recent years. There are exclusive suppliers for a small number of raw materials, but since these raw materials go into only a limited number of Frutarom products (none of which being substantial) out of its wide range of over 30,000 products, in the view of Company management Frutarom's dependence on these suppliers is not material.

28.3. Frutarom seeks to reduce costs of raw material used for the manufacture of its products and secure their ongoing supply by purchasing raw materials directly from the source through strengthening its global procurement capabilities in countries abounding with the necessary resources, like China, India and Brazil, expanding its pool of suppliers, and tightening its ties with manufacturers, processors and growers of raw materials.

Procurement of raw materials used in manufacturing the products of both of the Group's business activities is done with the support of the global headquarters supply chain unit, leveraging the purchasing power inherent in bulk purchasing to score favorable prices. Frutarom is working on reinforcing its global purchasing system and exploiting the growth of its purchasing power that has ensued largely from its recent acquisitions which have significantly increased its scope of activity.

28.4. The Group carefully manages its global supply chain and works towards strengthening its relations with manufacturers, processors and growers of raw materials, particularly natural raw materials, in order to ensure availability of raw materials at its various production facilities. Frutarom maintains relatively large inventories of certain raw materials as most of the natural substances used by Frutarom derive from field crops. Delivery times are also usually longer than those to which Frutarom has committed to its customers, making it necessary for Frutarom to hold enough raw material inventory to fill its customers' orders on short notice. On the other hand Frutarom generally maintains very limited finished goods inventory. Furthermore, the availability and prices of many of the raw materials, especially natural materials, used by Frutarom to manufacture its products are subject to fluctuations due to global supply and demand.

After several years of prices continually rising significantly for most of the raw materials used by Frutarom, price levels generally began to stabilize in 2013 and 2014. Frutarom closely monitors the prices of raw materials used in the manufacture of its products and, when the need arises, takes measures to prevent increases in raw material prices from impacting on its operating results. These might include adjustments to sale prices on products affected by the rise in raw material prices, expanding its pool of supplier, and making full and optimal use of the capabilities of its production sites around the world.

29. Working Capital

Frutarom’s working capital is composed of cash and cash equivalents, accounts receivable, debit balances and inventories; less short-term bank credit and loans and current maturities of long-term loans, and accounts payable and credit balances. For further information see the Company’s balance sheet in its financial statements.

30. Investments

30.1. The Group's capital expenditures go primarily towards enlarging and expanding existing facilities, developing new cutting-edge and more efficient manufacturing facilities, investing in environmental protection, and for establishing new sales and marketing offices and R&D laboratories.

30.2. Most of the investment planned by the Group in upcoming years is related to upgrading existing production facilities, improving their efficiency, and amalgamating production sites, along with continued implementation of a new company-wide IT system and improving and expanding production at Frutarom facilities, as well as investing in the areas of ecology, energy conservation and environmental protection.

The Company is building a new plant in China for producing both sweet and savory flavors which will also house state-of-the-art laboratories for development and applications. Construction started at the beginning of 2014 and ended in the first quarter of 2015, and the plant is slated to go into operation at the end of the second quarter of 2015.

In 2012 Frutarom received approval from the Ministry of Industry and Trade to build a new plant in Israel which will expand the Company's scope of R&D and production in Israel and globally, and will serve as a research and development center for natural products. The new plant will be located in Gilboa, a national priority area and, under Israel's Encouragement of Investments Law, it has won approval for a Development Area "A" investment grant and tax benefits. The investment grant will amount to at least 20% of the Company’s investment on fixed assets. The plant will be situated on land covering 64,000 square meters. Investment for building the new Gilboa plant is expected to stand at around US$ 30 million. During 2014 the Company was engaged in detailed planning for the new site and memoranda on environmental effects and surveys on risks were submitted as required to the Ministry of Environmental Protection and the Gilboa Regional Council. The Company intends to begin work developing the site during 2015.

30.3. The balance of the depreciated cost of property, plant and equipment net of investment grants on the Company's balance sheet as at December 31, 2014 stood at US$ 198.8 million. For further information on the Company's investment in fixed assets see Note 7 to the financial statements.

30.4. Company management believes the cash flow generated from operating activity will cover the required capital expenditure and working capital needs for the Company's internal growth over the next several years.

31. Financing

31.1. Frutarom's activity is financed by equity and long- and short-term loans from banks. The average and effective interest rate on the loans in force during the reported period was 1.39%.

31.2. During 2014 Frutarom used long-term loans from banks for financing acquisitions it has made in recent years. As of December 31, 2014 the net balance of debt to banks stood at US$ 167.5 million. For further information regarding loans taken by the Group from banks in 2014, see Notes 9 and 14 to the financial statements.

31.3. Frutarom has acted and is acting to improve the terms of loans it has taken in line with changing market conditions. Pursuant to this, in

November 2014 the Group prolonged a loan it had received from a Swiss banking consortium for funding acquisitions with a loan equaling € 60 million for a period of four years at a more favorable interest rate which varies according to the Company's results. There has been no material change in the conditions of the loan or any changes to the Company's financial covenants, as stated in section 31.4 below.

31.4. As part of an update of the credit facility at its disposal, the Company's financial covenants were updated on February 16, 2012 as follows:

- The Company's equity will at no point of time amount to less than US$ 300 million. As of December 31, 2014, the Company's equity stood at US$ 522.0 million.

- The Company's equity will at no point of time be equal to less than 35% of the Company's balance sheet. As of December 31, 2014 the Company's equity was equal to approximately 55.5% of the Company's total balance sheet.

- The ratio of debt net of cash to EBITDA shall not exceed 4.25. As of December 31, 2014 that ratio stood at 1.1.

As of the date of this report, the Company meets its financial covenants.

The Company has a negative pledge on its assets (in addition to the existing negative pledge on the assets of subsidiary Frutarom Ltd.). The Company has also committed to a restriction on dividend distributions under which it is entitled to distribute:

1) Up to 50% of the retained earnings accumulated up until December 31, 2011 as this figure appeared in the Company's balance sheet relating to December 31, 2011 (that is: US$ 270.3 million).

2) Up to 50% of the Company's annual net income in each calendar year as this figure appears in the Company's annual financial statements relating to same calendar year in which said net income was accumulated.

For further details on the aforementioned commitments to meet financial covenants, the negative pledge and restrictions on dividend distributions, see Note 14 to the financial statements and the Company's immediate report on the matter dated February 16, 2012.

31.5. In light of Frutarom's capital structure and solid balance sheet, supported by the strong cash flow generated over recent years, as of now Frutarom is not engaged in contractual credit facility agreements with banks and has no floating charges on its assets. The Group has understandings with leading banks around the world for being able to finance rapid growth and strategic acquisitions as the need arises.

31.6. Company management believes that it will not be required to raise funds in the coming year for running its ongoing activities.

31.7. For further details on the Company's loans, see Note 9 to the financial statements.

32. Taxation

32.1. For details of tax provisions applicable to the Company see Note 13 to the financial statements.

32.2. The Company has received final tax assessments in Israel for up to and including 2009.

32.3. The Company operates throughout the world and, as of the date of publication of this report, the applicable tax rates in the countries in which it operates range from 13% to 42%. For details on the Company's affiliated companies incorporated abroad see Note 13 to the financial statements.

32.4. The effective tax rate (on a consolidated basis) for 2014 was 19.5% compared with 19.7% in 2013. For a breakdown of differences between the Company's statutory tax rates and its effective tax rates see Note 13 to the financial statements.

33. Environmental Risk Management

Environmental Hazards

As of the date of publication of this report, Frutarom has 37 plants worldwide engaged in producing of flavors and specialty fine ingredients which includes the use and production of substances considered hazardous. These plants are therefore subject to different local legislation and regulations related to the environment and prevention of environmental hazards.

33.1. Environmental hazards which may materially affect the Group are:

33.1.1. The emission of substances from the manufacturing activity at a number of the Company's production facilities which may harm humans and the environment if reaching the surroundings in excess of permitted volumes or concentrations, including annoying smells that could reach the point of becoming an odor nuisance as defined by relevant local legislation. The Company takes the necessary measures in preventing uncontrolled emissions of such substances in accordance with provisions of the applicable law in each country in which it operates.

33.1.2. Production, maintenance and use at a number of the Company’s production facilities of materials defined as hazardous by the applicable local legislation (including flammable substances) which, if uncontrolled for any reason, may harm humans or the environment. The Company keeps these substances in accordance with the provisions of applicable law and takes the safety precautions that are necessary in using these substances.

Material Implications of Regulations

33.2. IPPC directive (96/61`/EC) (“**the Directive**”) went into effect in the European Union on October 30, 2007. The Directive establishes strict standards for everything relating to the prevention of environmental hazards and is enforced on the Group's sites in Europe.

On January 1, 2008 the Clean Air Law 5768 – 2008 (“**Clean Air Law”**) came into effect in Israel, adopting the principles of the Directive and applying them to plants defined as “emissions sources that require a permit.” As the Company’s plant in Haifa is an “emissions source that requires a permit,” as defined in the Clean Air Law, Frutarom submitted an application for an emissions permit, and it is possible that under the framework of the terms of the emissions permit, the Haifa site will have to comply with environmental demands and additional designated fees compared to those which were applicable to date by law. On March 1, 2015 the Company received a draft of the emissions permit for review. A final permit has not yet been issued.

Material Legal and Administrative Proceedings Related to the Environment

33.3. During the period of the report and until the date of its publication, no material legal or administrative proceedings were pending against the Company, or to which a Company officeholder was party, in connection with environmental issues.

The Group's Policy on Environmental Risk Management

33.4. Frutarom has and continually takes measures to prevent environmental hazards and protect the environment. The Company has been certified within the framework of the Responsible Care program. Company management keeps constant watch over the issue of environment protection and acts to reduce environmental risks at all Group locations.

Environmental trustees have been appointed at Frutarom's key production sites around the world as part of the implementation of the Group's strategic program for environmental protection. The trustees have undergone training for raising involvement and awareness for environmental protection by the workforces at all Group sites.

All of the Group's sites hold the licenses relevant to the legislative systems in their countries and, in the Company's assessment, are acting in accordance with the law.

33.5. Following is a list of the main actions taken by Frutarom in 2014 for reducing the risk of environmental hazards:

- According to the addendum to the Environmental Arrangement Document agreed upon in Israel between the Environmental Protection Ministry and the Company in June 2011, a process of transfer of production of a number of materials having an odor potential took place over the course of 2014, from the Company’s site in Haifa to a production site outside of Israel.

- At the Company's sites in Stuttgart, Germany and Reinach, Switzerland, all types of solid waste (organic waste, waste from the packing stage, plastic, carton and wood) are sent for recycling and reuse.

- At the Company's site in Wadenswil, Switzerland, an electric power station has been operating for a number of years. It operates on natural gases produced from the organic waste resulting from the production process.

- At the Company's site in Reinach, Switzerland a heat recycling system has been operating for a number of years, leading to a significant reduction in energy consumption.

- At the Company's site in New Jersey, USA, a multi-year program for handling the site's sewage discharge is in place in cooperation and with the approval of the relevant authorities in the USA. As part of the program, the construction process of a closed sewage discharge system and the upgrade of sewage discharge facilities and additional activities related to the plant's infrastructure were completed at the end of 2010, preventing contact between rainwater and the plant's sewage. In addition, an alcohol recycling system from organic waste and from the extraction process was installed and has been in operation since 2010, leading to a reduction of approximately 30% in alcohol waste which requires organized disposal.

- At the Company's sites in Northern UK a great emphasis is put on the recycling of methanol and ethanol in production processes and thus a significant reduction of the volume of waste is achieved. In addition, organic materials are sent to the production of compost and thus they help the environment.

- At the Company's site in China an air purification system was installed to reduce the emission of odors.

Material Environmental Amounts, Provisions and Costs

33.6. During the period of the report and until the date of its publication, no significant sums were awarded against the Company in connection with environmental matters.

33.7. The total amount spent by the Company in 2014 on environmental costs stood at US$ 2.9 million. This was spent on preventing and reducing environmental hazards and does not include investments carried out by the Company at its facilities as stated above. The Company does not foresee a significant change in the above costs during 2015.

34. Limitations and Supervision of the Company's Business

34.1. The Company develops, produces and markets its products in a number of countries throughout the world and is subject to the legislation, regulations and supervision applicable to its activities in each of the various countries. These laws and regulations include, among others, the U.S. Food and Drug Administration's (FDA) regulations regarding activity in the United States, EU directives implemented in the member countries of the European Union in which the Company operates, CODEX in South America and other countries, and regulations set by the Ministry of Health in Israel. These laws and regulations determine standards relating to food production and labelling, as well as to the production facilities, equipment and personnel required to produce products for human consumption.

34.2. The Company is also subject to various rules relating to health, work safety and environment at the local and international levels in the various countries where it operates. The Company's production facilities in the various countries are subject to environmental regulations concerning air pollution, sewage treatment, the use of hazardous materials, waste treatment and clean-up of existing environmental contamination. Environmental law and enforcement throughout the world have become more stringent in recent years and the costs of abiding by these laws have risen significantly.

34.3. Frutarom believes that it currently operates its facilities in compliance with the relevant laws and regulations for food manufacturing, work safety, health and the environment.

34.4. For further information on regulation, health, safety and permits, see section 13.10 of this report.

35. Material Agreements and Cooperation Agreements

35.1. For details regarding the Company's commitment to meet its financial covenants towards financing banks, see section 31.4 of this report.

35.2. For details regarding material bank loans taken on by the Group, see Note 9 to the Company's financial statements.

36. Legal Proceedings

36.1. For details regarding legal proceedings in which the Company is involved, see Note 11(b)(2) to the financial statements.

36.2. The Company is not involved in any significant legal proceedings in which the amount claimed (without interest and expenses) exceeds 10% of its current assets based on its consolidated financial statements.

37. Goals and Business Strategy

Frutarom's strategic objective is to achieve rapid and profitable growth, combining rapid profitable internal growth for its core businesses along with carrying out strategic acquisitions and strengthening its position as one of the world's top companies in the field of flavors and specialty fine ingredients, in fulfilling its vision:

"To be the Preferred Partner for Tasty and Health Success"

The key elements of Frutarom's strategy are as follows:

37.1. **Increasing the share of its Flavors' activity** – The successful implementation of Frutarom's rapid and profitable growth strategy has allowed Frutarom to significantly increase the share of its Flavors activity, the more profitable of its activities, achieving a higher rate of growth than the growth rate of markets in which it operates. Sales in this field now account for 72% of total Frutarom sales (as compared to 33% of total sales in 2000). The Company believes this rapid growth trend will also continue under the challenging market conditions through, among other things, the addition of products and the offer of comprehensive solutions to Company customers combining taste and health solutions, natural colors and natural food protection solutions.

37.2. **Developing new products and solutions combining taste and health** – Frutarom develops innovative taste and health solutions to suit customer requirements and future needs. These solutions provide a response for the main needs and major trends in the global food market and include combining taste and health, medical supplements, anti-aging products and food products designated for certain populations and age groups. The added value offered by Frutarom to its customers and its unique abilities in combining solutions for taste, texture and ingredients with supplementary health qualities give the Company an important competitive edge among customers in both developed and emerging markets. Most of these new products carry higher margins and therefore contribute not only to sales growth but also towards improving Frutarom's product mix and profitability.

37.3. **Focus on natural products** – Frutarom is working towards developing and expanding its portfolio of natural products in response to consumer demand and to major trends in the global food market for healthier and more natural foods. This field is growing at a fast pace and Frutarom's capabilities give it a competitive edge. In line with this strategy, Frutarom recently expanded its activity by also entering the natural food colors field (by acquiring Montana Food, Vitiva, and Ingrenat) and by substantially expanding its activity in the area of natural antioxidants that promote food protection.

37.4. **Improvements in the Specialty Fine Ingredients product mix** – Over the past few years Frutarom has worked towards improving its product mix in its Specialty Fine Ingredients activity as well. Frutarom's R&D teams have successfully developed innovative specialty natural products targeting both the realm of flavors and the realm of health. The successful penetration of these products contributes to higher sales for the Specialty Fine Ingredients activity along with improved margins. Frutarom is working on continuing to improve results from its Specialty Fine Ingredients activity also from new and innovative products currently in the development pipeline and those it will gain from its recent acquisitions.

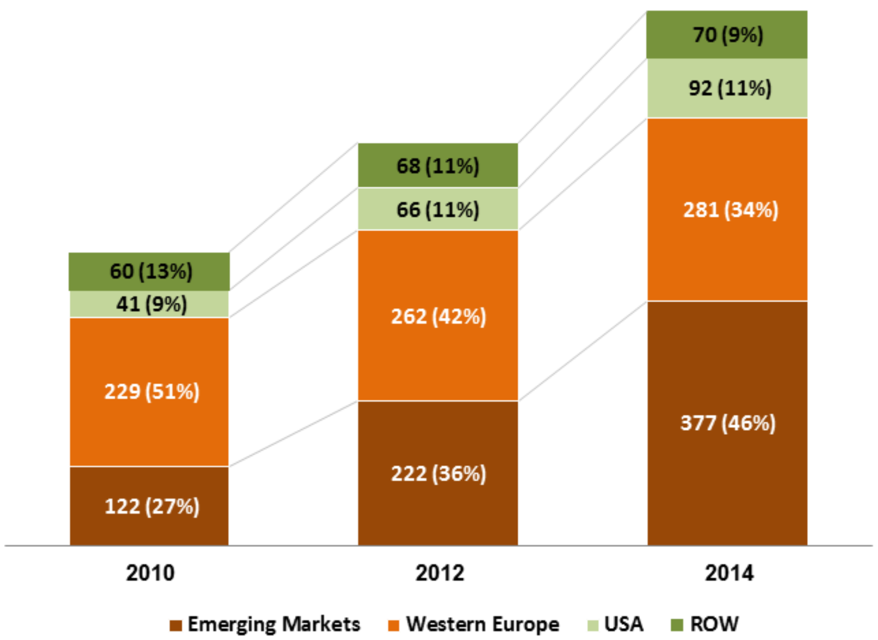
37.5. **Strategic changing of the geographic mix** – The successful implementation of Frutarom's strategy over the past few years, which includes among other things major expansion in the scope of sales and market share in emerging markets with higher growth rates as well as in the United States, has resulted in Frutarom sales for 2014 tripling in emerging markets and doubling in the US compared to

2010. At the same time the Flavors activity in the US has grown six-fold.

The rapid growth in activity outside of Western Europe has led to sales in Western Europe (which grew 23% compared to their level on 2010) making up 34% of total Frutarom sales in 2014 compared with 51% in 2010. Sales in emerging markets accounted for 46% of Frutarom sales in 2014 compared with 27% in 2010.

The six acquisitions made by Frutarom in 2013 and 2014 (JannDeRee in South Africa, PTI in Russia, Aroma in Guatemala, Hagelin in the United States - with sales also in Africa and in Latin America, US-based CitraSource and Montana Food in Peru and Chile) contribute and will continue contributing to Frutarom’s accelerated growth and to raising its sales and market share in emerging markets and in the United States in the coming years. Sales in emerging markets now make up close to 50% of Frutarom's total sales.

Frutarom focuses and will continue to invest heavy resources on accelerating growth and increasing the share of its sales from emerging markets and the US by, among other things, focused strengthening of its R&D, production, marketing and sales systems in important target countries and continuing to carry out further strategic acquisitions. At the same time Frutarom continues and will continue to also expand its activity in Western European markets, leveraging its broad product portfolio and continuing to capitalize on cross-selling opportunities.



37.6. **<u>Focus on providing quality service and product development to large multinational customers and medium sized local customers</u>** – Frutarom continues to expand the services it provides its customers as well as its portfolio of products and solutions, for both large multinational customers and mid-size local customers, with special emphasis on the fast growing private label market.

- In the market segment consisting of large multinational food and beverage manufacturers, Frutarom will continue to focus on providing niche products and on expanding its portfolio of natural solutions.

- In the mid-size and local customer segment of the market, Frutarom offers the same high level of service as generally provided to large multi-national customers, with products and solutions tailored to the customer's specific requirements. Frutarom also offers mid-size and local customers as well as its private label customers, usually with more limited resources than large and multinational customers, assistance in the development of their products while providing market support and flexibility on minimum order quantities and delivery dates.

37.7. **<u>Acquisitions and mergers and their contribution to the achievement of profitable growth</u>** – Frutarom has extensive experience performing acquisitions and mergers and works towards integrating the acquired companies and activities into its existing business while exploiting the inherent commercial and operational synergies in order to fully capitalize on the abundant cross-selling and cost savings opportunities and achieve continued improvement in its profit margins.

After having made five strategic acquisitions in 2011 and three at the beginning of 2012, all of which were successfully integrated with its global activities and contribute to both revenues growth and improved profitability, Frutarom has continued realizing its acquisition strategy with a focus on expansion of its sales and market portion in emerging markets, and in 2013 acquired the South African JannDeRee, the Russian PTI, the Guatemalan Aroma and the American Hagelin.

In 2014 Frutarom acquired CitraSource in the US and the Peruvian Montana Food with operations in Peru, Chile and other countries in the region. The integration of these six acquisitions is proceeding successfully and according to plan while the most is being made of the many cross-selling opportunities and operational, marketing and technological synergies that these acquisitions provide. Furthermore, at the beginning of 2015 Frutarom acquired Vitiva in Slovenia, FoodBlenders in the UK and Ingrenat in Spain, and is working to successfully integrate them and fully capitalize on the on the great potential they present.

<u>Increased Profits and Profit Margins</u>

37.8. In recent years Frutarom has succeeded in attaining, along with revenue growth, significant growth in gross and operating profits and margins. Frutarom strives and will continue to strive to strengthen its competitive abilities while raising its profits and margins by focusing, among other things, on the following objectives:

- **<u>Successful integration of acquisitions while maximizing synergies</u>** – Integration of the eight acquisitions made in 2011 and 2012 was completed successfully and as planned, and these acquisitions are contributing and will continue to contribute to Frutarom's sales growth and to improvement in profits and margins. Frutarom continues taking steps towards realizing the abundant cross-selling opportunities arising from the acquisitions, gaining maximum benefit from the many additional technological capabilities attained through them, and to capitalize on the savings from integrating the R&D, sales, marketing, supply chain, operations and purchasing functions. Integration of the six acquisitions made in 2013 and 2014 is moving ahead successfully. These acquisitions contribute and will continue contributing to Frutarom's ongoing growth in sales and profits this year and in the years to come. The successful integration of the three acquisitions performed at the beginning of 2015 (Vitiva, Ingrenat and FoodBlenders) is expected to also contribute to the continued trend of improvement in Frutarom's results.

- Investing in R&D for **specialized natural products in the fields of taste and health** that contribute to improvement of the product mix and Frutarom's profitability.

- **<u>Integration of R&D platforms</u>** – Frutarom strives to reap maximum benefit from the abundant research, development, innovation and technological capabilities gained over the last few years through its acquisitions, and to implement a new shared cross-organizational system for managing customer relations and R&D projects and applications with the aim of expanding the product portfolio, improving the quality of solutions and level of service to customers, with the channeling of projects to the relevant knowledge centers and leveraging of the knowhow and expertise developed at the various Frutarom locations over the past decades.

- **<u>Building up and strengthening global purchasing platform</u>** – Frutarom continues to build and strengthen its global purchasing system, leveraging the growing purchasing power attained with recent acquisitions and further expanding its pool of suppliers with an emphasis on increased purchase of raw materials used in the manufacture of its products from their countries of origin (especially natural raw materials). Integration of the R&D systems also contributes to the strengthening of the global purchasing capacities by capitalizing on the harmonization of the raw materials and the suppliers used by Frutarom in the development and manufacture of its various products.

37.9. **Efficiency plan** – Frutarom continues to implement and execute further projects for amalgamating and consolidating production sites and activities and also for attaining maximum purchasing, logistic and supply chain efficiencies that will contribute to strengthening its competitive position and improve its profits and margins in the coming years.

Frutarom expects that the continued execution of its rapid and profitable growth strategy combining profitable organic growth and strategic acquisitions, along with the contribution of its ongoing streamlining efforts and improvement of its costs structure, optimal utilization of its productions sites throughout the world, the bolstering of its global purchasing system and the successfully integration of recent acquisitions it has and will carry out, will result in a continuing trend of improved profit and margins. The Company expects its strategic plan for the next five years will lead to the achievement of reaching its target of surpassing US$ 1.5 billion in sales with an EBITDA margin of over 22% in its core businesses (given the current product mix) by 2020.

38. Financial Data Regarding Geographic Regions

The Group manufactures, markets, and sells its products throughout the world.

38.1. Following is the distribution of the Company's consolidated revenues by sales from unaffiliated end customers according to their geographic location (in US$ thousands):

38.2.

	2012	2013	2014	% of total 2014 Sales
Emerging markets	222,525	267,957	376,410	45.9%
Western Europe**	262,479	264,205	280,898	34.3%
USA	63,906	66,799	91,590	11.2%
Other	69,091	74,732	70,649	8.6%
Total	618,001	673,693	819,547	100%

* Sales in Russia reached US$ 165.6 million, US$ 89.9 million and US$ 54.5 million in 2014, 2013 and 2012 respectively.

** Sales in Germany amounted to US$ 72.6 million, US$ 71.9 million and US$ 74.1 million in 2014, 2013 and 2012 respectively.

38.3. <u>Data according to geographic location of main production sites</u>:

38.3.1. Following is a breakdown of sales according to geographic location of main production sites (in US$ thousands):

	2014				2013				2012			
	Flavors	Raw Materials	Elimin-nations	Total	Flavors	Raw Materials	Elimin-ations	Total	Flavors	Raw Materials	Elimin-ations	Total
Europe	433,703	55,692	(2,301)	487,095	367,725	57,056	(2,255)	422,526	338,907	57,840	(1,020)	395,727
Americas	68,654	33,085	(145)	101,594	44,001	27,066	-	71,067	40,050	27,719	-	67,769
Israel	46,262	38,837	(1,093)	84,016	46,650	37,742	(1,146)	83,246	46,399	33,587	(1,083)	78,903

* Sales are presented according to Geographic location of the manufacturing site net of sales of products manufactured at other Frutarom sites in other geographic regions.

38.3.2. Following is a breakdown of operating margins by division and geographic location of main production sites (%):

Flavors Division	2014	2013	2012
Divisional operating margin	16.5%	13.9%	13.0%
Europe	23.6%	14.4%	14.0%
Americas	22.4%	19.1%	18.0%
Israel	20.5%	23.9%	19.8%

Specialty Fine Ingredients Division	2014	2013	2012
Divisional operating margin	12.3%	11.8%	8.8%
Europe	9.7%	13.3%	8.4%
Americas	9.0%	3.4%	3.4%
Israel	23.7%	22.5%	13.4%

38.3.3. Total assets (without intercompany balances) by geographic location of main production sites (in US$ thousands):

	2014	2013	2012
Europe	488,989	540,084	459,503
Americas	177,220	167,131	113,240
Israel	72,314	71,811	67,435

38.4. For further information on geographic segments see Note 6 to the Financial Statements.

39. ***Discussion of Risk Factors***

Following is an outline of the main risk factors:

Macroeconomic Risk Factors

- **Effect of the global economy on Group activities**

  Due to the nature and type of its global activity, Frutarom is exposed to fluctuations in the global economy. Economic crisis and recession in important target countries could curb demand for the Company's products (mainly premium products) and significantly slow down the development and launch of new products by Frutarom customers. A global financial crisis could impair Frutarom's ability to raise funds for executing its strategic acquisitions. In recent years we have witnessed economic uncertainty in world markets, especially in Europe including some countries of the Eurozone, where signs of financial crisis have been apparent and have even led some into recession.

- **Stability in emerging markets**

  Frutarom operates in a number of countries besides the United States and Western Europe, such as Russia, the Ukraine, Turkey, Slovenia, Kazakhstan, China, countries in South and Central America (Brazil, Guatemala, Peru, Chile and Mexico) and countries in northern, southern and western Africa, and is therefore exposed to political, economic and legal developments in these countries which are generally less predictable than in developed countries. The Group's facilities in these countries could be subject to disruption as a result of economic and/or political instability as well as from nationalization and/or expropriation of assets situated there. There is also substantial risk relating restrictions on the Company to collect payment from its customers, distributors, or agents, as well as foreign exchange restrictions which could impede the Company's ability to realize its profits or to sell its assets in these countries. While none of the emerging market countries in which Frutarom operates impose foreign exchange restrictions that affect the Group, such restrictions did exist not long ago and there is no certainty that they will not be reinstated sometime in the future.

- **Currency fluctuations**

  About 70% of Frutarom's sales are conducted in currencies other than the US dollar (mainly the Euro, Pound Sterling, Swiss Franc, Russian Ruble, New Israeli Shekel, Chinese Yuan, Brazilian Real, Peruvian Nuevo Sol and South African Rand) and changes in exchange rates affect Frutarom's reported results in US dollar terms. However, exposure to currency fluctuations is reduced by the fact that Frutarom's raw materials purchases and operational expenditures in the various countries in which it operates are also paid for in most cases in the various currencies so that most of the effect applies to the translation of sales revenues and profits into dollar terms (and not to the profitability of its various activities and/or the group's profitability).

However, in cases of sharp fluctuations in exchange rates, and since a large part of the raw materials used in the manufacture of Frutarom's products are paid for in US dollars, in Euros, or other currencies, there is no certainty that the Company can completely update its selling prices denominated in local currency (which is different from the currency used in buying the raw material) and maintain its margin, and this could have considerably adverse implications for the Group's business, the results of its activity, and its financial condition. Most monetary balances which are not in dollars are the result of the local activity of subsidiaries operating in countries where the functional currency is not the dollar, and therefore the translation differences on local currency balances of each company do not have any effect on the Group's financing expenses and they are attributed directly to the translation differences capital fund. The monetary balances in other currencies are attributed to financial expenses. The currency exposure is examined whenever necessary and at least once every quarter. The Company has not undertaken any external hedging activity and does not use other financial instruments for protection against changes in exchange rates. For further information, see Note 3(a) to the Company's December 31, 2014 financial statements.

- **Changes in interest rates**

  For details regarding risks from changes in interest rates, see Interest Risks in Part B under Exposure to and Management of Market Risks in the Directors' Report, and Note 3(a) to the financial statements.

Industry-Related Risk Factors

- **Competition in markets where the Group operates**

  Frutarom faces competition from large multinationals as well as medium-sized and local companies in many of the markets in which it operates. Some of the Company's competitors have greater financial and technological resources, larger sales and marketing platforms and more established reputations, and may therefore be better equipped to adapt to changes and industry trends.

  The global market for flavors is characterized by close relations between flavor manufacturers and their customers, particularly with regard to large multinationals. Furthermore, large multinational customers, along with medium-sized customers too of late, limit the number of their suppliers and work exclusively with a list of "approved suppliers." To compete more effectively under these conditions, Frutarom must invest more resources in customer relations, in R&D and in matching products to customers' needs in order to provide good and efficient service. Any failure to maintain good relations with its customers, forge strong relations with new customers, or secure the status of "approved supplier" with some of its customers could lead to substantial adverse effects on the Group's business, operational results and financial condition.

The specialty fine ingredients market is more price sensitive than the flavors market and is characterized by relatively lower profit margins. Some fine ingredients products manufactured by the Company are less unique and more replaceable by competitors' products. Production overcapacity for fine ingredients globally could also negatively impact Frutarom’s sales and profitability. Although, as part of its strategy, the Company focuses on specialty fine ingredients with higher profit margins, there is no certainty that operating margins will not erode in the future, something which could substantially impact the Group’s business, operational results and financial condition.

- **Effect of regulatory changes on the Group**

  Frutarom is subject to a variety of international and domestic health, safety and environmental statutes in the various countries in which it operates. In general there is a trend towards increased regulation in the fields of the Group's activities resulting from growing consumer sensitivity concerning the inclusion of flavor additives in food products and the fact that regulators perceive nutraceuticals and functional food products as having medicinal attributes, and in some countries such products may come under the same standards and regulations as applied to drugs. Frutarom has identified the nutraceutical and functional food markets as important to its future growth. The subjecting of these markets to increased regulation could give rise to additional expenses which might have an adverse effect on the Company’s business, operational results and financial condition.

- **Compliance with environmental, health and safety regulations**

  Companies like Frutarom that operate in the flavor and fine ingredients industry make use of, manufacture, sell, and distribute substances that are sometimes considered hazardous and are therefore subject to extensive regulation concerning the storage, handling, manufacture, transport, use and disposal of such substances and their components and byproducts. This is particularly relevant to Frutarom’s production and R&D activities in the UK, Switzerland, Germany, Italy, the US, Israel, Russia, Slovenia, China, Spain, Brazil, Guatemala and other countries where operations are subject to various regulations and standards relating to air emissions, sewage treatment and the use, handling and discharge of hazardous material as well as clean-up of existing environmental contamination. Any further tightening of such laws and regulations could have a substantial adverse effect on the Group's business, operational results and financial condition.

  In addition to covering its ongoing environmental compliance costs, the Company might also incur nonrecurring charges associated with remedial action needed to be taken at its production sites. As environment-related incidents cannot be foreseen with any certainty, the sums that the Company allocates or will allocate for such matters may turn out to be inadequate. Ongoing and nonrecurring environment-related expenses could both have substantial adverse effects on the Company's business, operational results and financial condition.

Frutarom is required to obtain various permits related to the environment concerning operations at its various production facilities and to meet the conditions set by these permits. The expansion of existing plants is also subject to securing necessary permits. Such permits might be unilaterally revoked or modified by the issuer, or expire after a given length of time. Any cancellation, modification and/or failure to renew or obtain a permit could have a significant adverse effect on the Company's business, operational results and financial condition.

- **Exposure to civil and criminal liability with respect to environmental, health and safety laws and regulations applicable to the Group**

  The laws and regulations concerning the environment, health and safety may involve Frutarom in civil and/or criminal liability for non-compliance or environmental pollution. Environmental, health and safety laws may include criminal sanctions (including substantial penalties) for violating them. Some environmental laws also include provisions imposing complete responsibility for the release of hazardous substances into the environment which could result in Frutarom becoming liable for clean-up efforts without any negligence or fault on its part. Other environmental laws impose liability jointly and severally, something which could expose the Group to responsibility for cleaning up environmental pollution caused by others.

  In addition, some environmental, health and safety laws are applied retroactively and could impose responsibility for acts done in the past even if such acts were carried out in accordance with the relevant legal provisions in force at the time. Criminal or civil liability under such laws may have significant adverse effects on the Company's business, operational results and financial condition.

  Frutarom may also become subjected to claims for personal injury or property damage arising from exposure to hazardous substances. Laws in the major countries where the Group operates permit legal proceedings to be instituted against it if personal injury or environmental contamination was ostensibly caused by activity at its production sites in these countries. Such legal proceedings could also be instituted by private individuals or non-governmental organizations.

- **Fluctuations in prices of raw materials needed for producing the Group's products**

  For details on risks from fluctuations in prices for raw materials required for producing Frutarom products, see Raw Material Price Risks under Exposure to and Management of Market Risks in the Directors' Report.

- **Reliance on exclusive raw material suppliers and availability of natural raw materials**

  Frutarom is dependent on third parties for the supply of raw materials needed manufacturing its products. Although the Group purchases raw materials from a very wide range of suppliers and no individual supplier accounts for more than 10% of its total raw material usage, and even though there is more than one supplier for most of the raw material bought by the Group and they are usually readily available, there is no certainly that this will also continue to be the case in the future. Severe weather conditions may cause a significant shortage for natural raw materials used by the Company. A shortage of these raw materials could impair Frutarom sales for a certain period of time.

- **Damages awarded from possible claims due to product warranty**

  Frutarom is exposed to product liability risk, particularly due to the fact that it supplies flavors to the food and beverage, flavor and fragrance, functional food, pharma/nutraceutical and personal care industries. Should the Company be found responsible in a large claim of this type, its insurance coverage might be inadequate for covering damages and/or legal expenses. A lack of adequate insurance coverage could result in significant adverse effects on the Company's business, operational results and financial condition. Product liability claims brought against the Group could might damage its reputation as well as put heavy demand of the management's time and efforts, and this could have significant adverse effects on the Company's business regardless of the outcome of the claim.

<u>Risk Factors Unique to the Group</u>

- **Frutarom's future ability to pinpoint, acquire and integrate suitable businesses**

  A key element in Frutarom's growth strategy is growth through the acquisition of flavor and specialty fine ingredients manufacturers. In line with this strategy, Frutarom has made many strategic acquisitions of companies and business activities in recent years. There can be no certainty, however, that Frutarom will be able to continue pinpointing suitable acquisitions on satisfactory terms or obtain the necessary for continuing with such acquisitions. Any failure to identify and execute future acquisitions could adversely impact the Company's growth strategy.

The integration of acquired activities involves a number of risks, including possible adverse effects on the Group’s operating results, loss of customers, diversion of senior management’s time and attention, and failure to retain key personnel, along with risks associated with unanticipated events in the integration of the operations, technologies, systems and services of the acquired business. In addition, Frutarom may be unable to capitalize on the anticipated synergies (including those aimed at cost savings) inherent in such acquisitions. Failure in successfully integrating its acquisitions could have adverse effects on the Company’s business, operational results and financial condition.

- **The rapid growth characterizing the Group's activity in recent years**

  The rapid growth, as in recent years, in both the Group's activities and its geographical spread requires effective management to ensure that the financial benefits, tapping of synergies and the economies of scale are achieved. An inability to adapt effectively to the rapid growth could result in losses or acquisition costs that will not recovered as quickly as anticipated, if at all. Such circumstances could have significant adverse effects on the Company’s business, operational results and financial condition.

- **Hiring and retaining key employees**

  The Company’s continued future success depends on its ability to attract and retain proficient flavorists (flavor developers), lab technicians and other skilled personnel. The Company operates in a highly specialized market where product quality is of critical importance and having skilled personnel is necessary for ensuring the supply of high quality products. If a number of such employees were to leave at the same time, the Company could encounter difficulties in finding replacements with equivalent experience and abilities, a situation which could impair the Group's R&D capabilities. Furthermore, Frutarom’s continued success depends to a large extent on its senior management team. The loss of services from members of senior management or other key employees could have a negative impact on Frutarom’s results and its ability to implement its strategy. A failure to recruit and retain skilled personnel or members of senior management could have a significant adverse effect on the Company’s business, operational results and financial condition.

- **Protection of intellectual property**

  The Group’s business relies on intellectual property, mainly consisting of formulas used to create its flavors. Frutarom does not register these formulas but they are kept highly confidential and considered trade secrets and, as such, are accessible to just a very limited circle of people within the Group. Although Frutarom believes it is not significantly reliant on any individual intellectual property right, proprietary formula, patent or license, a breach of confidentiality with respect to the formulas or loss of access to them and/or the future expiration of intellectual property rights could have a significant adverse impact on the Group's business, operational results and financial condition.

Frutarom relies, in part, on confidentiality agreements, ownership of intellectual property, and non-competition agreements with employees, vendors and third parties in order to protect its intellectual property. It is possible that these agreements will be breached and that Frutarom may lack an adequate remedy for any such breach. Disputes may arise concerning the ownership of intellectual property or the extent to which the confidentiality agreements remain in force. Furthermore, the Company's trade secrets may become revealed to its competitors or developed independently by them, in which case the Company will not be able to enjoy exclusive use of some of its formulas or maintain confidentiality concerning its products.

Following is a table outlining the various risk factors and the Company's evaluation concerning their possible effect:

Risk Factor	Risk factor's level of impact on the Company		
	High	Medium	Low
Macroeconomic Factors			
Effects of the global economy		✓	
Stability in emerging markets		✓	
Currency fluctuations		✓	
Changes in interest rates		✓	
Industry Related Factors			
Competition in the markets		✓	
Regulatory changes		✓	
Compliance with regulations		✓	
Exposures to liabilities		✓	
Fluctuations in raw materials prices		✓	
Reliance on exclusive suppliers and availability of natural raw materials		✓	
Awards for damages without adequate insurance coverage		✓	
Factors Unique to the Group			
Pinpointing future acquisitions		✓	
Adapting to rapid growth		✓	
Hiring and retaining key employees		✓	
Protection of intellectual property			✓

40. ***Details about Valuations***

40.1. Following are details about the valuation of the savory activity in Germany in accordance with Accounting Standard IAS36 and the provisions of Regulation 8b to the Securities Regulations (Periodic and Immediate Reports), 1970:

Valuation subject	Goodwill of the savory activity (Germany, UK, Norway, Italy)
Valuator	BDO Ziv Haft Consultants and Management Ltd.
Valuation requester	Frutarom Industries Ltd., by Mr. Guy Gill, VP Finance
Engagement date	December 2014
Approval to attach to reports	The valuator gave written approval to attach the valuation to the Company's reports
Valuation timing	Goodwill value as of December 31, 2014. Valuation was conducted in February and March 2015.
Value of goodwill prior to valuation date	€142,072 thousand
Value of goodwill according to valuation	€158,289 thousand
Identification of evaluator and its characterization	Ziv Haft Consulting and Management was established by partners in the BDO Ziv Haft Accounting firm. Ziv Haft Consulting and Management is part of the global BDO network and provides consulting and management services in a wide variety of areas for companies operating in different areas. The company has rich experience in the following areas: valuations, due diligence – financial and accounting) valuation of goodwill and intellectual assets, performance of financial analysis, current analysis of Israeli public hi-tech and communications companies, business plans, planning of presentations for potential investors, financial management and analysis of BOT and PFI projects, receivership, liquidation and appointment as special administrator, handling companies in crisis, formulating recovery plans, management of business and companies, supporting mergers and splits, transaction planning and more. Evaluator: Tzach Kasuto Evaluator's education • BA in Economics, Tel Aviv University

	• MBA, Tel Aviv University Experience and expertise: • Performance of financial assessments and valuations, including valuations for accounting needs of reporting corporations and in similar scopes to those of the reported assessment or greater; • Pricing and analysis of financial issues for government and private bodies; • Support in IPOs and consultation in mergers. The valuator is has no dependence on Frutarom and there are no indemnification agreements with the valuator.
Valuation Model	• DCF (discounted cash flow).
Valuation Assumptions	• Discount rate before taxes: 14.6% • Long term growth rate: 2.5% • Sensitivity to growth: 1.5% to 3.5% • Discount rate sensitivity: 12.6%-16.6% Data used as a basis for comparison: the activity's results in recent years and its forecast.
Prior Valuation	• Valuation dated December 31, 2013 conducted by Ziv Haft Consultants and Management Ltd., signed on March 18, 2014. Value of activity according to the above valuation was €142,072 thousand.

40.2. Details about the valuation for the Flavors Activity_in the United States in accordance with Accounting Standard IAS36 and the provisions of Regulation 8b to the Securities Regulations (Periodic and Immediate Reports), 1970:

Valuation subject	Goodwill of the flavors activity in the United States
Valuator	BDO Ziv Haft Consultants and Management Ltd.
Valuation requester	Frutarom Industries Ltd., by Mr. Guy Gill, VP Finance
Engagement date	December 2014
Approval to attach to reports	The valuator gave written approval to attach the valuation to the Company's reports
Valuation timing	Goodwill value as of December 31, 2014. Valuation was conducted in February and March 2015.
Value of goodwill prior to valuation date	US$102,743 thousand
Value of goodwill according to valuation	US$188,736 thousand
Identification of evaluator and its characterization	Ziv Haft Consulting and Management was established by partners in the BDO Ziv Haft Accounting firm. Ziv Haft Consulting and Management is part of the global BDO network and provides consulting and management services in a wide variety of areas for companies operating in different areas. The company has rich experience in the following areas: valuations, due diligence – financial and accounting) valuation of goodwill and intellectual assets, performance of financial analysis, current analysis of Israeli public hi-tech and communications companies, business plans, planning of presentations for potential investors, financial management and analysis of BOT and PFI projects, receivership, liquidation and appointment as special administrator, handling companies in crisis, formulating recovery plans, management of business and companies, supporting mergers and splits, transaction planning and more. Evaluator: Tzach Kasuto Evaluator's education • BA in Economics, Tel Aviv University • MBA, Tel Aviv University

	Experience and expertise: • Performance of financial assessments and valuations, including valuations for accounting needs of reporting corporations and in similar scopes to those of the reported assessment or greater; • Pricing and analysis of financial issues for government and private bodies; • Support in IPOs and consultation in mergers. The valuator is has no dependence on Frutarom and there are no indemnification agreements with the valuator.
Valuation Model	• DCF (discounted cash flow).
Valuation Assumptions	• Discount rate before taxes: 13.8% • Long term growth rate: 2.5% • Sensitivity to growth: 1.5% to 3.5% • Discount rate sensitivity: 12.8%-14.8% Data used as a basis for comparison: the activity's results in recent years and its forecast.
Prior Valuation	• Valuation dated December 31, 2013 conducted by Ziv Haft Consultants and Management Ltd., signed on March 17, 2014. Value of activity according to the above valuation was $102,743 thousand.

Valuation

Savory Cash Generating Unit

As Of December 31, 2014

Frutarom Industries Ltd.

Impairment Study - Savory Cash Generating Unit

As Of December 31, 2014

February 2015

BDO Ziv Haft
Amot Bituach House Building B, 48
Menachem Begin Road, Tel Aviv
66180
Israel

Dear Sirs,

We were requested by Frutarom Industries Ltd. (Hereinafter: **“Frutarom”** or the **“Company"**) to perform an Impairment Examination Study (Hereinafter: the **“Study”**) of the Savory Cash Generating Unit (Hereinafter: the "**savory**" or the “**Unit"**) under the requirements of Statement of International Accounting Standards 36 (**IAS 36**). To the best of our knowledge there is no prevention, legal or other, to perform the Study enclosed herein.

Our findings will be used by Frutarom, its management and its critics, and those financial reporting purposes as part of the accounting principles and financial reporting practices in Israel and required by law, including in accordance with IAS 36 Impairment of Assets (IAS 36). This study is intended for the exclusive use of Frutarom, its management, independent critics only by law.

Based on our study, we have concluded that the Unit's Goodwill is not deemed to be impaired, as of December 31, 2013.

We know that this examination will be used and / or be included in the financial statements as stated in the regulations under the Securities Law - 1968. No other use of this opinion except for the above, including, quoted in full or parts of it, and can be transferred to third parties some, without the express written approval in advance.

In the course of our Annual Goodwill Impairment Test, we relied upon financial and other information, including prospective financial information obtained from Management and from various public, financial and industry sources. Our conclusion is dependent on such information being complete and accurate in all material respects.

This examination does not represent due diligence and does not purport to include the information, tests and exams or any other information included in due diligence.

We did not check the information independently, except for the fairness examination.

We performed a number of examinations:

• Analyzed business results of operations in recent years, making a fairness examination of revenue and expenditure forecasts used in this document;

• An examination of the expenses of operations;

• Review of operating profitability of operations.

Economic opinion is not an exact science, and should reflect a reasonable and fair condition as of a particular time, on the basis of known data, assumptions and forecasts that were determined. Changes in the factors and / or information, may change the underlying basic assumptions and in accordance with the conclusions. The calculations in this study were performed using a spreadsheet, so there may be rounding differences.

We wish to note that we have no personal interest in the company, we are independent of the Company or one of the Group as such term is defined in the auditors 1955 and the regulations promulgated thereunder. Also note that are no conditions for legal fees in connection with the results of this opinion.

For our study, we relied on data and documents, as follows:

- Management reports of operations for 2012-2014;
- Unaudited consolidated financial statements received from Frutarom's management based on the audited financial statements of operations;
- Forecasts for the years 2015-2019 operations;
- Barnea reports of Frutarom 2013;
- Financial and operational business, which was obtained by Frutarom's management;
- Information regarding Savory activities;
- Conversations with the company's management;
- Public data.

Based on our study and the findings set out in our general conclusion that the value of goodwill activity appears in the books did not decrease, and therefore does not require re-estimation and reduction of intangible assets of operations as shown below:

€000	2014
Recoverable amount	158,289
Carrying amount	125,234
Impairment amount	–

Only authorized personnel should have access to this document, any person who is not an official recipient of this report or who signed a letter of personal responsibility to BDO Consulting Group is not authorized to access this document. BDO is not responsible for unauthorized persons seeing this document or any other person obtaining this document. If an unauthorized person chooses to rely on the contents of this document, that person is solely responsible. Unauthorized person, who reads this document is required understand the following conditions:

• This document was prepared in coordination with the guidelines, provided by the recipient exclusively for personal use.

• BDO Consulting Group, its partners, employees and agents have no responsibility towards the reader or any damage caused (including commitment, negligence or responsibility), or otherwise. We are not obliged to discuss the basis of this document or the accuracy of its contents and information since the date of composing it. We are not responsible from any loss, damage or expense that resulted from any readers who have chosen to use or rely on this document.

• Our study was directed in coordination with the appropriate professional instructions. In other sectors, the relevant procedures and work practices may display data differently. This document was not conducted in coordination with the procedures and practices of any professional body.

• Do not refer to this document or cite it or parts of it, exposed to any other third party.

In forming our opinion we have relied on sources, which appeared to us as reliable, and nothing came to our attention, which is likely to indicate the lack of reasonability of the data we used. We did not examine the data in an independent manner and, therefore, our study does not constitute verification of the correctness, completeness or accuracy of the data.

Details regarding the valuation specialist

BDO Consulting and Management Ltd. were founded by the partners of BDO Certified Public Accountants.

BDO Consulting and Management is part of the international BDO network, provides a full range of business services required for national and international businesses in any sector. Our company has vast experience in the following fields: business valuations, financial and tax due diligence, goodwill and intangible assets valuations, financial analyses, business plans, project finance PFI/PPP advisory, M&A, investment banking and more.

Consulting & Management Ltd.

Respectfully submitted,

BDO Ziv Haft

Contents

Section 1
Cash Generating Unit Overview

BDO Ziv Haft Consulting Group

CGU Overview

General

As aforesaid, Savoy forms part of the flavouring activity department of Frutarom. Savory deals with the development, manufacturing, and marketing of Savory Taste Solutions (the non-sweet taste spectrum). Its product line includes flavors, seasoning compounds, and functional ingredients for the food industry, with a specialization in the processed meat, fish, and convenience food sectors.

These non-sweet flavors are used primarily in the production of snacks, salty pastries, processed meat and fish and convenience foods. Additionally, Savory produces unique seasoning mixes and functional ingredients for meat, poultry and fish processors, as well as a variety of flavors of meat substitutes designed to help impart meat flavor in vegetarian preparations.

In recent years, Frutarom has accelerated its targeted growth by implementing a strategy combining profitable organic growth and execution of strategic acquisitions in order to expand its business opportunities in both emerging and developed markets. In the last decade, Frutarom has significantly increased, both in terms of its savory sector mergers and its acquisitions activity.

Production Facilities

The following are the main production facilities of the Unit:

- **Sittensen, Germany (Nesse)** - At this plant the Company's flavor activity produces savory flavor mixes and seasonings.
- **Production Capacity and Shifts** - The plant operates five days a week in two shifts (excluding Friday, when there is one shift). The plant has additional potential production capacity of about 30%-35% assuming that it shifts to continuous production over three shifts.
- **Stuttgart, Germany (Gewurzmuller)** - At this plant the Company's flavor activity produces savory flavor mixes and seasonings. The plant is a modern, efficient enterprise, and meets the stringent standards of the European food industry.

  Production Capacity and Shifts - The plant operates five days a week in one shift. The plant has additional potential production capacity of around 100% assuming that it produces continuously over three shifts.
- **Stuttgart, Germany (Blessing) -** At this plant under the Company's flavor activity, starter cultures are produced.

  Production Capacity and Shifts - The plant operates five days a week in continuous production. The number of shifts and their duration corresponds with the volume of the production activity. The plant has additional potential production capacity of around 20%.

CGU Overview

Production Facilities

- **Parma, Italy – -** At this plant under the Company's flavor activity produces savory flavors.

  Production Capacity and Shifts - The plant operates five days a week in continuous production. The plant has additional potential production capacity of 100% assuming that it shifts to continuous production over three shifts.

- **UK Plants (SFLV, EAFI) –** There are two UK plants that operate in producing flavor concentrates, seasoning mixes, marinades and sauces, specializing in snacks and convenience foods.

Customers

The savory activity's' products sold to an extensive customer base comprised of thousands of large multinational, mid-sized, local and small customers. The customers are primarily food and they are located different countries worldwide.

The majority of sales are made to permanent customers. The savory activity is characterized by long-term relationships and customer loyalty.

Sales and Marketing

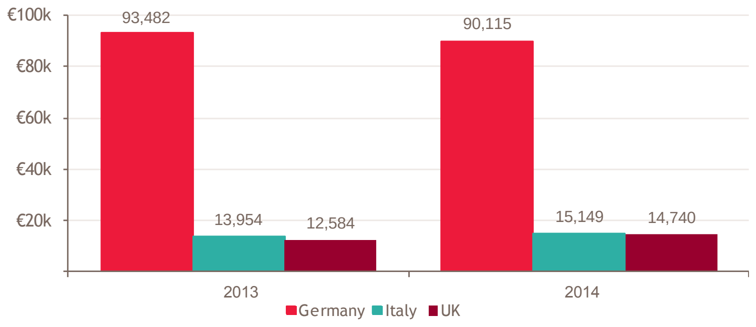
The Company markets and sells its products across a wide geographical area. Centers of activity are:

Germany - The German subsidiary has 20 local marketing points and sells units in 20 countries besides Germany, mainly in East and west Europe.

Norway - The River activity has a development and marketing facility in Norway, and a well range of customers, which includes leading food producers, mainly in the Scandinavia countries.

Italy - The CH activity has an extensive customer base in Russia, Ukraine, Poland, Czech Republic, in France and mainly among processed meat producers in Italy.

The following chart presents sales by production site for 2013 and 2014::



Source: Management information

CGU Overview

Balance Sheet

The following table presents the unaudited (see source below) balance sheet of the Unit as of December 31, 2014 (Thousands EUR):

€000	31.12.14
Current Assets	
Cash & cash equivalents	7,581
Accounts receivable	16,200
Other receivable	813
Inventory	19,945
Deferred tax asset	1,486
Total current assets	**46,025**
Long-term assets	
Net fixed assets	18,537
Net intangible assets	95,086
Long term inter-company balances	47,156
Total long-term assets	**160,778**
Total assets	**206,803**
Current liabilities	
Accounts payable	8,484
Other short-term liabilities	5,536
Other payables, related parties	3,831
Total current liabilities	**17,851**
Long term liabilities	
Inter Company loans	66,250
Pension liability	3,411
Deferred tax (PPA)	4,084
Total long term liabilities	**73,745**
Total liabilities	91,596
Total shareholder's equity	115,207
Total liabilities and equity	**206,803**

Source: Management information (unaudited consolidated financial statements for 31 December 2014, based on audited financial statements of the companies comprising the Unit

Profit & Loss

The following table present the profit and loss statements, of the Savory activity, in a full year performance, as of December 31, 2014 (Thousands EUR):

€000	2013	2014
Revenue	120,020	120,004
Growth rate	*8%*	*0%*
Cost of sales	80,616	80,634
% of revenue	*67%*	*67%*
Gross profit	**39,404**	**39,371**
Gross margin	*32.8%*	*32.8%*
R&D	4,670	4,761
% of revenue	*4%*	*4%*
S&M	13,786	14,652
% of revenue	*11%*	*12%*
G&A	6,957	6,453
% of revenue	*6%*	*5%*
Total operating expenses	25,412	25,866
% of revenue	*21%*	*22%*
Operating profit	**13,991**	**13,505**
Operating margin	*11.7%*	*11.3%*

Source: Management information (unaudited consolidated financial statements for 31 December 2014, based on audited financial statements of the companies comprising the Unit)

Section 2
Market Overview

Market Overview

Flavor and fragrance industry worldwide

The global market for flavors, fragrances and raw materials in 2012, was estimated at approximately $23 billion. Frutarom is not active in the fragrances market, but is active in the market of natural functional food ingredients (excluding the above estimate), and therefore, it believes to sell in the markets where it operates, approximately $18.5 billion. According to Leffingwell & Associates, Frutarom is ranked as one of the ten largest companies in the taste and smell markets.

In 2011, the research company IAL Consultants, estimated that sales in industrialized countries (USA and Western Europe) in the flavors markets, in which the Company operates, will grow at an annual rate of 2%, from 2012 to 2017. Frutarom estimates that sales of raw materials, in those markets, will grow at an annual rate, similar to the years 2015 to 2017. According to these estimates, the growth rate in emerging markets where the Company operates, such as Asia, Central and South America, Eastern Europe and Africa, is expected to be significantly higher due to changes in consumer preferences in these markets and the transition to processed food, and can reach average annual rates of 5.9% from 2012 to 2017.

The manufacturers of the flavor, fragrance and fine ingredient markets can be divided into three main groups: large multinational companies; mid-sized companies; and local and small companies.

Flavor and fragrance industry worldwide

Large multinational manufacturers generally operate globally and have revenues in excess of $ 1 billion. In the global flavor and fragrance markets there are five such manufacturers which, according to Leffingwell & Associates, represent approximately 60% sales in the flavor, fragrance and fine ingredients markets (excluding sales of natural functional food ingredients and pharmaceutical/nutraceutical extracts). These multinational manufacturers focus primarily on customers who are large multinational food and beverage producers.

Local and small companies generally have revenues of less than $ 100 million (most of them are much smaller and sell only several million dollars). The Company estimates that in the global flavor and fragrance markets, there are approximately 500 such companies that, according to the estimation of Leffingwell & Associates, represent approximately 10% of the value of the flavor, fragrance and fine ingredients market (again excluding sales of natural functional food ingredients and pharmaceutical/nutraceutical extracts). These companies generally focus on smaller local customers and have limited capabilities in the areas of service, research and development and innovation.

Mid-sized companies, such as Frutarom, have revenues between $ 100million and $1 billion. In the global flavor and fragrance markets there are only eight such mid-sized companies. According to the estimation of Leffingwell & Associates these eight companies represent approximately 30% of the value of the flavor, fragrance and fine ingredients market (excluding sales of natural functional food ingredients and pharmaceutical/nutraceutical extracts). Some of these mid-sized players focus heavily on specific geographic markets (such as the USA, France and Japan).

Market Overview

Flavors market

Flavors are the key building blocks that impart taste in processed food and beverage products and, as such, play a significant role in determining the consumer acceptance of the end products in which they are used.

The research company IAL Consultant, estimates that global 2012 sales of flavors for the industry amounted to approximately US $ 8.7 billion. Flavor products are sold primarily to producers of prepared food, beverage, dairy, bakery, meat and fish, confectionery and pharmaceutical products.

The following are examples of end user products using flavors:

- **Beverages** - carbonated, noncarbonated, sport and functional, alcoholic and juices.
- **Dairy** - yogurt, drinking yogurt, ice cream, cheese and chilled desserts.
- **Bakery** - cakes and cookies, crackers and cereals.
- **Confectionery** - candy, chocolate, jam and chewing gum.
- **Savory and convenience food** - ready meals, instant soup, ready sauces and instant noodles.
- **Snacks** - potato chips and other savory snacks.
- **Meat** - sausages and frankfurters.
- **Processed Fish**.
- **Oral hygiene and pharmaceuticals** - toothpaste, mouthwash, vitamins and medicines.
- **Others** - animal feed and pet food and tobacco.

The global market for flavors has expanded rapidly over the last 60 years, primarily as a result of an increase in demand for, as well as an increase in the variety of, consumer end products containing flavors. The demand for consumer goods containing flavor products has increased as a result of rapid population growth and consumer preferences resulting from various factors such as increases in personal income, leisure time, health concerns and urbanization.

Market Overview

Flavors market

These factors have led to an overall increase in food and beverage products containing flavors and to rapid growth in demand for convenience food and foods with healthier and more natural content..

The following table sets forth the sales of flavors by region in 2012 and the projected annual growth rate in these geographic regions:

Country	World consumption in 2012 ($ million)	Average growth is expected in 2012-2017	Market share
Western Europe	1,712	1.30%	19.75%
Eastern Europe	585	2.70%	6.75%
North America	2,470	2.40%	28.49%
South America	651	7.60%	7.51%
Asia	2,652	6.20%	30.59%
Middle East and Africa	599	5.30%	6.91%
Total	**8,669**	**4.10%**	**100.00%**

According to the estimates above, the largest flavor market in 2012 was the Asian market representing approximately 30.6% of the global market, followed by North America with approximately 28.5%. The South American market had the most significant expected growth rate (7.6%) followed by the Asian market with estimated annual growth rate of about 6.2% in 2012-2017.

Flavors market - Characteristics

The following are the characteristics of the Flavor Market:

- **Reliable with high levels of service** - Food and beverage producers, the principal customers of flavor manufacturers, expect reliable, high-quality service to meet their needs in terms of support and lead time, while maintaining high quality, regulatory and safety standards. These requirements encourage the formation of long-term relationships between flavor producers and their customers. As a result, large multinational customers, and increasingly also mid-sized customers, have pruned the flavor suppliers that they will work with, placing those that remain on "core lists" creating a barrier to entry for small flavor manufacturers.
- **Research and development** - The development of flavor products in general and of new flavor extracts in particular is a complex, creative and technological process that calls for depth of knowledge and skill on the part of a flavor manufacturer's research and development personnel. Effective research and development is critical in ensuring a continuous stream of innovative products and in maintaining the profitability and growth of a flavor manufacturer. The initiative for the development of new flavor products can be spurred by the flavor manufacturer or by the customer who is in need of a specific flavor for use in a newly developed end product. As such, in order to anticipate market demands, a flavor manufacturer's research and development personnel are required to be familiar with the taste requirements of various end product types and target markets. In addition, as most flavors are tailor made for a specific customer, a close collaborative relationship with the customer is essential. These flavor formulas are treated as commercial secrets and remain the proprietary asset of the flavor manufacturer.

Market Overview

Flavors market - Characteristics

As most flavor products are tailor-made for a customer, customers are less likely to replace suppliers for such flavor products during the course of the end products' life cycle.

- **Low price sensitivity** - Since flavor products play a major role in determining the flavor of the end product to which they contribute, they are a vital element of its success. Flavor products cannot be precisely matched and their cost, compared to the total cost of the end products, is negligible. When selecting a flavor supplier, a customer will generally place a greater emphasis on the reputation, innovation, service, quality and consistency of the supplier than on the price of its flavors. The demand for flavors is therefore generally less sensitive to changes in price.
- **Production processes** - Flavor products in general and flavors in particular typically contain a variety of ingredients (typically over 30 per flavor), which are blended using unique formulas created by a manufacturer's flavor expert. The production processes involved in the manufacture of flavor products are less complex and capital intensive compared to those of fine ingredients. However, the production process for flavor products requires skill and knowhow to achieve the required consistency and quality.
- **High and relatively stable profitability** - As the flavors market tends to be characterized by long-term relationships and high customer loyalty, combined with relatively low price sensitivity and simple production processes, it generally benefits from high and stable margins. This is true also in comparison to the fine ingredient industry.

Flavors market - Characteristics

Flavors are sold primarily to food and beverage producers; therefore the flavor market is generally driven by trends characterizing the demands of food and beverage consumers.

According to Data Monitor, global sales in the food and beverage market amounted to $ 4,650 billion in 2012. Frutarom estimates that over 60% of such total global sales are generated by mid-sized, local and small food and beverage producers. Although there has been a general trend towards consolidation in the food and beverage industry, Frutarom estimates that mid-sized (annual revenues of between $100 million and$ 1 billion) and local and small (annual revenues of below $100 million) food and beverage producers will continue to play a significant role in the market, and that new mid-sized, local and small producers will continue to emerge.

- The large multinational flavor manufacturers often focus on large multinational food and beverage producers, offering their customers a high level of service and tailor-made product development. Frutarom believes that these flavors producers focus to a lesser extent on mid- sized and local customers, offering limited service and offering less customizable product offering to these customers.

Market Overview

Food and Beverage Market - Characteristics

However, the Company believes that mid-sized and local food and beverage producers require the same level of service and tailor-made products as their larger counterparts, and also require short lead times and manufacturing flexibility. Small, localized flavor producers generally do not have the product variety and service capabilities to support the needs of these customers. A specific example of this type of customer is the private label customer. This situation creates a business opportunity for mid-sized flavor producers to service this segment.

Food and Beverage Market - Tendencies

The following are the main trends in the consumer market for food and beverages which in turn drive the flavor market:

Local and global tastes - Taste preferences vary by geographic location and among different cultures. Flavor manufacturers must have thorough knowledge of local tastes in each of the countries in which they are active. It is also important for a global flavor manufacturer to have a physical presence in its key target markets in order to facilitate direct contact with customers, to better understand local tastes and to be able to respond quickly and efficiently to changes in consumer preferences. Additionally, the trend toward globalization now characterizes the flavor industry as multinational food and beverage customers are now launching global brands in many different markets simultaneously, often by changing the taste profile to meet the preferences of the respective populations worldwide.

Food and Beverage Market - Tendencies

- **Preference of natural products** - There has been a general increase in consumer demand for food and beverage products containing natural ingredients and having dietary values (reducing fat, salt, cholesterol, etc.). Natural products are generally perceived by consumers as being of higher quality, healthier and more environmentally friendly. Similarly, there is growing demand for organic products and ‘clean label’ products. As a result, natural food and beverage products are viewed as specialty, premium products that can command higher prices. This trend has created new opportunities for flavors manufacturers to develop new and innovative natural flavor products.
- **Continuously growing consumption of convenience food** - There is an increase in demand for processed foods with greater convenience (consumed both inside and outside of the home). This increase in demand for convenience foods has been spurred by new packaging and cooking technologies as well as changing social habits and consumer preferences. Examples of convenience foods include "ready to eat" meals, fresh pasta; ready-to-cook, fresh seasoned or marinated meat or poultry; salads; and sauces in liquid form. This has created new opportunities for flavor manufacturers in the savory flavors and functional fine ingredients fields which are responsible for the creation of food texture and its extended shelf life, to develop and market flavors and unique fine ingredients products for this segment.

Market Overview

Food and Beverage Market - Tendencies

- **Private label** - private label goods manufacturers, which tend to be mid-sized, local or small food manufacturers, are a growing customer segment in the flavor industry. Over the last decade consumers of food products have become increasingly price conscious, increasing sales of private label products in comparison to the branded food and beverage industry. This trend was accelerated in 2009 as a result of the economic crisis. As a result, supermarket chains and other retailers have been increasing their private label product offerings.
- **Emerging markets** - In recent years, certain developing markets, such as Asia, Central and South America, Eastern Europe and Africa have experienced above-market-average growth in demand for flavors products. Further, these markets have been characterized by a trend towards increased consumption of processed foods, which in turn has driven the emergence of mid-sized, local and small food companies, creating new market opportunities for flavor manufacturers.

Food and Beverage Market - Critical Success Factors

The critical success factors in the flavor segment are:

- **Long-term relationships** - Long-term relationships with customers and collaboration in the development of new products.
- **Global and local presence in target markets** - Knowledge of the various flavor preferences in the different markets and the ability to provide global and local support to customers.
- **Superior and reliable service** - The ability to provide a high level of service and the reliability of a flavors manufacturer in giving service are critical for mid-sized, local customers and multinational customers.
- **Presence in emerging markets** - Emerging markets grow at considerably higher rates in comparison to developed markets. Presence in these key areas, along with knowledge and understanding of their unique needs and the ability to provide support to local manufacturers is a critical success factor.
- **Innovation in research and development** - The ability to develop innovative products both at the initiative of the flavor manufacturer and in collaboration with customers is of extreme importance.
- **Compliance with strict quality, regulatory and safety standards** - Since the flavors are intended principally for the food and beverage and pharmaceutical markets, they must comply with strict quality, regulatory and safety standards

Market Overview

Food and beverage market - Critical Success Factors

- Procurement of raw materials –there is a growing importance in diverting resources to targeted procurement in countries that are an important source of raw materials, such as China, India and Brazil, while expanding the pool of suppliers, reducing costs through an efficient global procurement network and strengthening relationships with producers, processors and growers of raw materials, will provide a secure and reliable supply and improve procurement costs..

Flavors Market - Competition

In the flavor market, Frutarom's main competitors consist of large global manufacturers, mid-sized companies and smaller, local manufacturers. Competition is based to a large extent on innovation, product quality, the ability to provide the customer with added value, and establish and maintain long term customer relationships, value added service, reliability and development of products which are tailor made for the customers' needs and the future market directions. As the cost of flavors accounts for only a small percentage of the total cost of an end product, this market tends to display low price sensitivity. Flavor manufacturers must differentiate themselves by maintaining close collaborative relationships with customers, thorough knowledge and understanding of target markets, innovative abilities, effective research and development and an established reputation for consistent, reliable and effective service, product supply and quality, and the ability to supply product on short notice and with short lead time.

Flavors Market - Competition

Large multinational flavor manufacturers are established, experienced companies with a global presence and established technical and commercial capabilities, focusing primarily on large multinationals customers. The large multinational flavors producers with whom Frutarom competes include Givaudan, Firmenich, IFF Inc., Symrise and Takasago.

The midsized flavors manufacturers with whom Frutarom competes, focus on both large multinational food and beverage producers as well as and mostly on mid-sized and smaller food and beverage producers who tend to operate in smaller geographical regions. Mid-sized flavor manufacturers with whom Frutarom competes include Sensient, Mane, Robertet, Kerry Ingredients, Wild and Dohler.

The Company estimates that there are approximately 700 small and local flavor manufacturers with more limited research and development capabilities who focus on narrow market segments and local customers. In recent years there has been a trend towards consolidation in the flavor manufacturing industry, resulting in increasing market concentration.

Market Overview

Risks Factors

The risks of the global market of flavors, fragrances and fine Ingredients refers to macroeconomic risks and to risks related to the Industry.

Risks Factors - Macroeconomic Risks-

The following are the main macroeconomic risk factors:

- **The effect of the global economy on the Company's activities** - Due to the nature of its global activity, Frutarom is exposed to fluctuations in the global economy. Economic crisis and recession in important target countries may cause dips in demand for the Company's products (mainly for premium products) and significantly slow down the development and launch of new products by the customers.
- **Stability in emerging markets** - Companies who operates in a number of countries outside of Western Europe and the United States, such as Russia, Turkey, Kazakhstan, Ukraine and China, is generally exposed to the political, economic and legal systems and conditions in these countries which are generally less predictable than in developed countries
-

Risks Factors - Macroeconomic Risks

- **Currency fluctuations** - The Company has sales, expenses, assets and liabilities denominated in currencies other than the U.S. due to that fact, fluctuations in the exchange rates of these foreign currencies could have an impact on a Company's results of operations.
- **Changes in interest rates** - The Company's sources of banking finance, as needed, for short and long term, are linked to different coins, according to the activity currency of the subsidiary, and bear Libor interest at variable rates in accordance with its policy. Therefore, if interest rates increase, the Company may not be able to refinance its credit agreements, or any other indebtedness, on attractive terms. Increases in interest rates will impact the Company's cash flow.

Market Overview

Risks Factors - Industry Risks

- **Extensive competition -** Companies in the global market of flavors, fragrances and fine Ingredients face increased competition both from large multinational and mid-sized companies as well as smaller local companies in many of the markets in which they operates. Some of the competitors have greater financial and technological resources, large sales and marketing organizations and great name recognition, and may therefore be better able to adapt to changes and trends in the industry. The global market for flavors is characterized by close, collaborative relationships between flavor manufacturers and their customers, particularly in the large multinational customer segment.
- **Changes in regulations -** Companies are subject to a variety of health, safety and environmental rules at national, state and local levels in the various countries in which it operates. Generally, there is a trend towards increased regulation in the industry in which the Group operates. This has been a result of increased public sensitivity toward the composition and use of flavor products and from the fact that as a result of their medicinal qualities and claimed health benefits, nutraceutical and functional food products are being increasingly viewed by regulators as having similar characteristics to pharmaceutical products, which may lead their subject to the regulatory framework governing the market for pharmaceutical products.

Risks Factors - Industry Risks

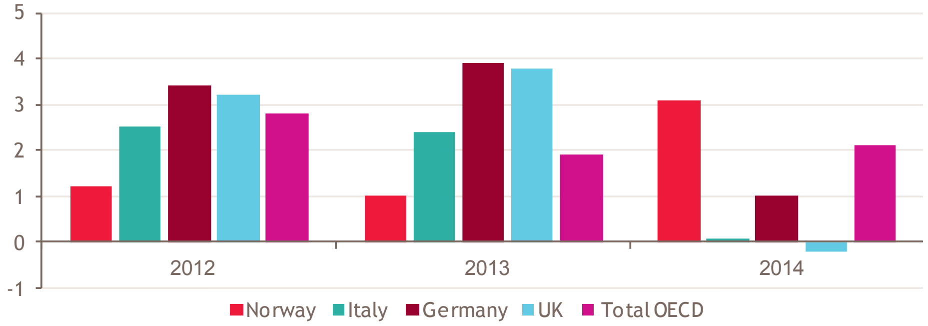
- **Environmental, health and safety regulations** - Companies in the flavor and fine ingredients industry also use, manufacture, sell and distribute a number of environmentally hazardous materials, and therefore are subject to extensive regulation regarding the storage, handling, manufacture, transportation, use and disposal of their products, ingredients and byproducts. Any increase in the stringency of applicable environmental regulations could have a material adverse effect on companies business, results of operations or financial condition.

Fluctuations in prices of raw materials - The last few years were characterized by relatively high fluctuations in the prices of raw materials used by companies in the flavor and fine ingredients industry, to manufacture its products. The global increase in demand for raw materials in general, and raw materials for the food industry, in particular, continues and strengthens in recent years. Source of the increase in demand is mainly in third world countries, which populations rapidly change their consumption habits. In addition, the raw materials market is affected by the food industry, which, in recent years, experiences a decrease in supply, which comes from damage to crops in different countries, arising from extreme and prolonged drought and floods. The phenomenon of decrease in supply is exacerbated by the increasing diversion of crops, such as wheat and soybeans, for corn and other crops which are sugar producers, which are now used to create ethanol and other materials which produce Bio Diesel.

Market Overview

Risks Factors - Industry Risks

Increased demand with supply reduction is usually translated into an increase in commodity prices. The following graph shows the rates of increase in food prices, as presented by the OECD, between the years 2012-2014:



Section 3
Methodology

Methodology

IAS 36 - General

The International Accounting Standard 36 Impairment of Assets (hereinafter "IAS 36") objective is to prescribe the procedures that an entity applies to ensure that its assets are carried at no more than their recoverable amount. An asset is carried at more than its recoverable amount if its carrying amount exceeds the amount to be recovered through use or sale of the asset. If this is the case, the asset is described as impaired and the Standard requires the entity to recognize an impairment loss. The Standard also specifies when an entity should reverse an impairment loss and prescribes disclosures.

This Standard shall be applied in accounting for the impairment of all assets (other than exceptions as they appear in the standard content) or cash generating unit(s) including goodwill acquired from business combination. Goodwill acquired in business combination represents the value of the intangible assets which cannot be separately identified or separately recognized. Goodwill does not generate cash flow independently from other cash-generating unit(s), and often contributes to the cash flows of several cash-generating units. The Standard requires goodwill acquired in a business combination to be tested for impairment as part of impairment testing of the cash-generating unit(s) to which it relates, once a year or when there is a sign of impairment loss.

Definitions

The following terms are used in this Standard with the meanings specified:

Carrying amount is the amount at which an asset is recognized after deducting any accumulated depreciation (amortization) and accumulated impairment losses thereon.

A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are independent of the cash inflows from other assets or groups of assets.

Corporate assets are assets other than goodwill that contribute to the future cash flows of both the cash-generating unit under review and other cash-generating units.

Depreciation (Amortization) is the systematic allocation of the depreciable amount of an asset over its useful life. (In the case of an intangible asset, the term ‘amortization’ is generally used instead of ‘depreciation’. The two terms have the same meaning).

Fair value less costs to sell is the amount obtainable from the sale of an asset or cash-generating unit in an arm’s length transaction between knowledgeable, willing parties, less the costs of disposal.

An impairment loss is the amount by which the carrying amount of an asset or a cash-generating unit exceeds its recoverable amount.

The recoverable amount of an asset or a cash-generating unit is the higher of its fair value less costs to sell and its value in use.

Methodology

Definitions

a) The period of time over which an asset is expected to be used by the entity; or

b) The number of production or similar units expected to be obtained from the asset by the entity.

Value in use is the present value of the future cash flows expected to be derived from an asset or cash-generating unit.

Determining an Impairment Loss

The Standard defines number of steps for the identification, recognition and measurement of value loss of an asset or cash generating unit. Moving on to the next step is subjected to the fulfillment of the previous step.

Identifying an asset that may be impaired

An entity shall assess at each reporting date whether there is any indication that an asset may be impaired. In assessing whether there is any indication that an asset may be impaired, an entity shall consider, as a minimum, the following indications:

External sources of information:

- During the period, an asset's market value has declined significantly more than would be expected as a result of the passage of time or normal use.
- Significant changes with an adverse effect on the entity have taken place

Definitions

during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the entity operates or in the market to which an asset is dedicated.

- Market interest rates or other market rates of return on investments have increased during the period, and those increases are likely to affect the discount rate used in calculating an asset's value in use and decrease the asset's recoverable amount materially.
- The carrying amount of the net assets of the entity is more than its market capitalization.

Internal sources of information:

- Evidence is available of obsolescence or physical damage of an asset.
- Significant changes with an adverse effect on the entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used. These changes include the asset becoming idle, plans to discontinue or restructure the operation to which an asset belongs, plans to dispose of an asset before the previously expected date, and reassessing the useful life of an asset as finite rather than indefinite.
- Evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected.

Methodology

Determining an Impairment Loss

If any indication of value loss exists, the entity shall estimate the recoverable amount of the asset. In case the value of the recoverable amount found is lower than the respective Carrying amount, the entity shall depreciate the value of the asset or the Cash-generating unit accordingly.

The standard requires an intangible asset with an indefinite useful life or not yet available for use and goodwill to be tested for impairment, once a year, regardless to the existence of indication of value loss.

Measuring Recoverable Amount

The recoverable amount of an asset or a cash-generating unit is the higher of its fair value less costs to sell and its value in use.

The Standard prescribes that it is not always necessary to determine both an asset’s fair value less costs to sell and its value in use, where either of these amounts exceeds the asset’s carrying amount.

Furthermore, the Standard points out that there are cases where it is not possible to determine fair value less costs to sell of an asset, particularly when the asset is not traded in an active market. In such case, the entity may use the asset’s value in use as its recoverable amount.

Fair value less costs to sell

The best evidence of an asset’s fair value less costs to sell is a price in a binding sell agreement in an arm’s length transaction, adjusted for incremental costs that would be directly attributable to the disposal of the asset.

If there is no binding sell agreement but an asset is traded in an active market, fair value less costs to sell is the asset’s market price less the costs of disposal.

If there is no binding sell agreement or active market for an asset, fair value less costs to sell is based on the best information available to reflect the amount that an entity could obtain, at the end of the reporting period, from the disposal of the asset in an arm’s length transaction between knowledgeable, willing parties, after deducting the costs of disposal. In determining this amount, an entity considers the outcome of recent transactions for similar assets within the same industry.

Costs of disposal, other than those that have been recognized as liabilities, are deducted in determining fair value less costs to sell.

Methodology

Fair value less costs to sell, continued

Costs of disposal are incremental costs directly attributable to the disposal of an asset, such as legal costs and similar transaction fees, costs of removing the asset and direct incremental costs to bring an asset into condition for its sale (excluding finance costs and income tax expense).

Value in use

The following elements shall be reflected in the calculation of an asset's value in use:

- An estimate of the future cash flows the entity expects to derive from the asset;
- Expectations about possible variations in the amount or timing of those future cash flows;
- The time value of money, represented by the current market risk-free rate of interest;
- The price for bearing the uncertainty inherent in the asset; and
- Other factors, such as illiquidity, that market participants would reflect in pricing the future cash flows the entity expects to derive from the asset.

Estimating the value in use of an asset involves the following steps:

- Estimating the future cash inflows and outflows to be derived from continuing use of the asset and from its ultimate disposal; and
- Applying the appropriate discount rate to those future cash flows.

Measuring Recoverable Amount, continued

In measuring value in use an entity shall:

- Base cash flow projections on reasonable and supportable assumptions that represent management's best estimate of the range of economic conditions that will exist over the remaining useful life of the asset.
- Base cash flow projections on the most recent financial budgets/forecasts approved by management, but shall exclude any estimated future cash inflows or outflows expected to arise from future restructurings or from improving or enhancing the asset's performance. Projections based on these budgets/forecasts shall cover a maximum period of five years, unless a longer period can be justified.
- Estimate cash flow projections beyond the period covered by the most recent budgets/forecasts by extrapolating the projections based on the budgets/forecasts using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified. This growth rate shall not exceed the long-term average growth rate for the products, industries, or country or countries in which the entity operates, or for the market in which the asset is used, unless a higher rate can be justified.

When the carrying amount of an asset does not yet include all the cash outflows to be incurred before it is ready for use or sale, the estimate of future cash outflows includes an estimate of any further cash outflow that is expected to be incurred before the asset is ready for use or sale.

Methodology

Measuring Recoverable Amount, continued

Estimates of future cash flows shall not include estimated future cash inflows or outflows that are expected to arise from:

- A future restructuring to which an entity is not yet committed; or
- Improving or enhancing the asset's performance.
- Cash inflows or outflows from financing activities; or
- Income tax receipts or payments.

Future cash flows are estimated in the currency in which they will be generated and then discounted using a discount rate appropriate for that currency. An entity translates the present value using the spot exchange rate at the date of the value in use calculation

Discount rate

The discount rate (rates) shall be a pre-tax rate (rates) that reflect(s) current market assessments of:

- The time value of money; and
- The risks specific to the asset for which the future cash flow estimates have not been adjusted.

Cash-generating units and goodwill

For the purpose of impairment testing, goodwill acquired in a business acquisition will be allocated from the acquisition date for each cash-generating units or groups of cash-generating units of the acquirer, which are expected to benefit from the synergies of the acquisition, irrespective of whether other assets or liabilities of the acquiree are assigned to those units or groups of these units. Each unit or group of units to which goodwill has been allocated as mentioned above, will represent the lowest level of the entity in which goodwill is monitored for internal management purposes and not be larger than an operating segment as defined in the standard, IFRS 8 before the aggregation of similar segments.

Examination of Goodwill Impairment

Examination of goodwill impairment will be performed by comparing the book value of the unit, including goodwill, to its recoverable amount. If the recoverable amount of the unit exceeds the book value of the unit, goodwill allocated to the unit will be considered as not impaired. If the book value of the unit exceeds the recoverable amount of the unit, the entity shall recognize an impairment loss.

Methodology

Recognizing and measuring an impairment loss

If, and only if, the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset shall be reduced to its recoverable amount. That reduction is an impairment loss.

An impairment loss shall be recognized immediately in profit or loss, unless the asset is carried at revalued amount in accordance with another Standard.

The impairment loss shall be allocated to reduce the carrying amount of the assets of the unit (group of units) in the following order:

- (a) First, to reduce the carrying amount of any goodwill allocated to the cash-generating unit (group of units); and
- (b) Then, to the other assets of the unit (group of units) pro rata on the basis of the carrying amount of each asset in the unit (group of units).

In allocating an impairment loss, an entity shall not reduce the carrying amount of an asset below the highest of:

- (a) Its fair value less costs of disposal (if determinable);
- (b) Its value in use (if determinable); and
- (c) Zero.

Section 4

Examination of Goodwill Impairment

Examination of Goodwill Impairment

General

Determining an Impairment Loss

Frutarom's management requested that the examination of goodwill impairment will be carried out according to international accounting standards of IAS 36.

In accordance with IAS 36 annual examination of goodwill impairment of a cash-generating unit may be performed at any time during an annual period, provided the test is performed on the same date each year. Frutarom's management has determined the date of assessment of impairment of goodwill will be December 31 annually.

Identifying the cash-generating unit

In accordance with IAS 36, goodwill deriving from a business acquisition will be allocated to the cash-generating unit, which is expected to benefit from the synergies of the acquisition. The standard defines a cash-generating unit as the group of the smallest identifiable asset, generating cash inflows that are largely independent of the cash inflows from other assets. For additional details, see the methodology section.

Frutarom's management determined that Savory activities, is the smallest cash-generating unit which the goodwill arising from the acquisition can be assigned to..

General

The recoverable amount of the cash-generating unit

In accordance with IAS 36 the recoverable amount of the larger between cash-generating unit is fair value less costs of sales and its usage value, , additional details, see the methodology section.

To assess the value in use of the cash-generating unit, we estimate that the income approach, the discounted cash flow method (Discounted Cash Flows), is the most appropriate for the valuation. For more details on valuation approaches and methodologies, see Chapter valuation approaches.

Cash-generating unit book value

In accordance with IAS 36, the book value of the cash generating unit shall be consistent with the recoverable amount. The book value includes the book value of assets and liabilities that can be directly attributable to the cash-generating unit, which generates the future cash inflows that determines the value using the discount cash flow method.

In order to determine the book value of the cash generating unit we received from management the book value of Frutarom as of December 31, 2014. Due to the fact that the book value includes only operational assets and liabilities (excluding net financial liabilities and assets surplus), the recoverable amount of the cash generating unit was examined accordingly.

Impairment Examination of Goodwill

General

An analysis of the activity of the pro forma balance sheet shows that the book value of activity, as of December 31, 2014 is approximately 125,234 thousand Euros.

Impairment Examination of Goodwill

In accordance with IAS 36, impairment examination of goodwill will be performed by comparing the book value of the unit including goodwill to its recoverable amount. If the recoverable amount of the unit exceeds the book value of the unit, the unit and the goodwill allocated to the unit will be considered as not impaired. If book value of the unit exceeds the recoverable amount of the unit, the entity shall recognize an impairment loss.

Estimation of the recoverable amount

Measurement of the recoverable amount is determined by the value of operations. Valuation of operations will be based on the implementation of the three approaches, as described below. The approaches take into account the type of assets, the condition of the firm, and the information available to the analyst.

Income Approach

The income approach is based on the premise that the value of a security or asset is the present value of the future earning capacity that is available for distribution to investors in the security or asset. A commonly used methodology under the income approach is a discounted cash flow analysis. A discounted cash flow analysis involves forecasting the appropriate cash flow stream over an appropriate period and then discounting it back to a present value at an appropriate discount rate. This discount rate should consider the time value of money, inflation, and the risk inherent in ownership of the asset or security interest being valued.

Market Approach

The market approach references actual transactions in the equity of the enterprise being valued or transactions in similar enterprises that are traded in the public markets. Third-party transactions in the equity of an enterprise generally represent the best estimate of fair market value if they are done at arm's length. In using transactions from similar enterprises, there are two primary methods. The first, often referred to as the Guideline Transactions Method, involves determining valuation multiples from sales of enterprises with similar financial and operating characteristics and applying those multiples to the subject enterprise. The second, often referred to as the Guideline Public Company Method, involves identifying and selecting publicly traded enterprises with financial and operating characteristics similar to the enterprise being valued. Once publicly traded enterprises are identified, valuation multiples can be derived, adjusted for comparability, and then applied to the subject enterprise to estimate the value of its equity or invested capital.

Cost Approach

This method that surmises that the price someone should pay for an asset should not exceed what someone would have to pay to replace with an equivalent. In cost approach pricing, the market price for the asset is equivalent to the replacement value of the asset less depreciation. The use of this approach will be made especially in cases where there is no reliable information available and similar firms and / or was not

Impairment Examination of Goodwill

General

Possible to rely on future cash flow projections.

For this examination we will use the income approach using discounted cash flow method. According to this approach, we will build the future cash flows; the company is expected to make a reasonable scenario, based on the parameters, which are described below. Later, future cash flows are discounted at a pre-tax discount rate, which is suitable for the type of activity reflecting the proper risk level.

Revenues

The following table presents the Unit's estimated revenues according to our forecast and the actual revenue results, for the years 2013-2014 (thousands EUR)::

€000	2013	2014	2015	2016	2017	2018	2019	Terminal
Revenue	120,020	120,004	124,805	129,173	133,048	136,374	139,784	143,278
Growth rate	*8.0%*	*0.0%*	*4.0%*	*3.5%*	*3.0%*	*2.5%*	*2.5%*	*2.5%*

Source: BDO analysis and Management's projections

The Unit's revenues derived from two sub activities (Hereinafter all together: the **"Activity"**):

- The savory activity in Germany, 75% of the total Unit's revenue for 2014.
- The savory activity in Italy, 13% of the total Unit's revenue for 2014.
- The savory activity in the UK, 12% of the total Unit's revenue for 2014.

The savory activity has an extensive customer base which is mainly located in Israel and Europe, especially in Italy, Norway, Germany, Russia, Ukraine, Poland, Czech Republic, France, Austria and Switzerland.

During 2013 the Unit's revenue was approximately 120,020 thousand Euro. During 2014, revenue amounted to 120,004 thousand Euros. This year part of Russian production was transferred to domestic Savory operations in Frutrom Russia (acquired in Q4 of 2014) as an efficiency measure of Frutarom's management in response to the current situation in Russia that favors domestic production.

BDO Ziv Haft Consulting Group

Impairment Examination of Goodwill

Revenue projections

In order to determine the growth rate of the Unit's activity in 2014, we have conservatively examined Management's projections. Management foresees a growth rate of 4% according to the nature of the business and the projected growth rate for the industry. Management informs us it performed several procedures in order to increase operational efficiency, and is currently looking to establish and maintain increased growth rates.

The Company intends to continue focusing on its sales and marketing efforts, in order to achieve the estimated growth rates. Projected growth rates are based on the organic growth of the activity, particularly in light of mergers and acquisitions completed during 2013, which are expected to assist future growth trends with increased exposure to new markets and customers.

For the following forecast years, it was assumed that revenue will decrease from 4% in 2015, to a rate of 2.5% in the terminal year, representing the long-term growth rate of the Company.

Cost of Sales

The following table presents the Unit's estimated cost of sales according to our estimations, and the actual cost of sales results, for the years 2013-2014 (thousands EUR):

€000	2013	2014	2015	2016	2017	2018	2019	Terminal
Cost of sales	80,616	80,634	83,036	85,146	87,007	88,596	90,218	91,875
% of revenue	*67.2%*	*67.2%*	*66.5%*	*65.9%*	*65.4%*	*65.0%*	*64.5%*	*64.1%*

Source: Source: BDO analysis and Management's projections

Cost of sales include: costs of raw materials, salaries, depreciation and amortization and other expenses.

In 2013, cost of sales amounted to 80,616 thousand Euros. In 2014 these expenses were a total of 80,634 thousand Euros, representing about 67.2% of total revenues.

In light of the above, we have projected the total cost of sales in 2015 will decrease to 66.5% of revenue and will reach a level of approximately 65.4% in 2017 and up to 64.1% in the terminal year. In order to determine the projected cost we have analyzed the fixed and variable elements of the cost of sales structure, including the change in cost as a result of change in expected revenue. It was assumed in the long term cost of sales will increase according to the permanent growth rate.

Impairment Examination of Goodwill

Gross profit

The following table presents the Unit's estimated forecasted gross profit f and the actual gross profit results, for the years 2013-2014 (thousands EUR):

€000	2013	2014	2015	2016	2017	2018	2019	Terminal
Gross profit	39,404	39,371	41,769	44,027	46,041	47,778	49,565	51,404
Gross margin	*32.8%*	*32.8%*	*33.5%*	*34.1%*	*34.6%*	*35.0%*	*35.5%*	*35.9%*

Source: BDO analysis and Management's projections

As a result of the assumptions described above, the gross margin in the forecast will increase to approximately 33.5% in 2015 and will increase gradually with implementation of efficiency measures to about 35.9% in the terminal year.

Sales and Marketing

The following table presents the Unit's estimated S&M expenses according to our forecast, and the actual S&M expenses results, for the years 2013-2014 (thousands EUR):

€000	2013	2014	2015	2016	2017	2018	2019	Terminal
S&M	13,786	14,652	15,110	15,523	15,888	16,198	16,515	16,838
% of revenue	*11.5%*	*12.2%*	*12.1%*	*12.0%*	*11.9%*	*11.9%*	*11.8%*	*11.8%*

Source: BDO analysis and Management's projections

The Unit's S&M expenses consisting mainly of employee wages, advertising, commission's fee, overhead expenses and other expenses.

In 2013, S&M expenses of the Unit totaled to approximately 13,786 thousand Euros, representing about 11.5% of total revenues In 2014, these expenses.

In 2015, according to Management's forecast, it was assumed that sales and marketing expenses will be about 15,110 thousand Euros and will be about 12.1% of the Unit's revenue. The reduction of these costs, from the total revenues, reflects the Company's intention to continue the optimization process, as planned.

In order to determine the projected cost we have analyzed the fixed and variable elements of the S&M cost structure, including the change in cost as a result of change in expected revenue. This analysis shows that the rate of sales and marketing costs decreased gradually from 12.1% to 11.8% of revenue and will be at approximately 16,838 thousands of Euros in the terminal year. In the forecasts that this cost will increase in accordance with the long-term growth rate of operations.

Impairment Examination of Goodwill

General and Administrative

The following table presents the Unit's estimated G&A expenses according to our forecast, and the actual G&A expenses results, for the years 2013-2014 (thousands EUR):

€000	2013	2014	2015	2016	2017	2018	2019	Terminal
G&A	6,957	6,453	6,581	6,696	6,796	6,881	6,967	7,055
% of revenue	*5.8%*	*5.4%*	*5.3%*	*5.2%*	*5.1%*	*5.0%*	*5.0%*	*4.9%*

Source: BDO analysis and Management's projections

The Unit's G&A expenses consist mainly of relevant employee rent expenses, office expenses, vehicles expenses and other expenses.

In 2013, the G&A expenses were approximately 6,957 thousands of Euros, which reflect a rate of 5.8% of revenues. In 2014, the G&A expenses were about 6,453 thousand of Euros, which reflect a rate of 5.4% of revenues.

In 2015, Management expects a decrease in G&A costs, as a result of the operational efficiency procedures implemented. Accordingly, it was assumed the decrease trend will continue and G&A expenses will be about 6,581 thousand Euros, representing 5.3% of revenue, continuing the 2013-2014 trend.

In the forecast years it was assumed G&A expenses as a percentage of revenue will improve gradually to 4.9% of revenue. It was assumed in the long term G&A cost will increase according to the permanent growth rate.

Research and Development

The following table presents the Unit's estimated R&D expenses according to our forecast, and the actual R&D expenses results for the years 2013-2014 (thousands EUR):

€000	2013	2014	2015	2016	2017	2018	2019	Terminal
R&D	4,670	4,761	4,894	5,014	5,120	5,210	5,301	5,394
% of revenue	*3.9%*	*4.0%*	*3.9%*	*3.9%*	*3.8%*	*3.8%*	*3.8%*	*3.8%*

Source: BDO analysis and Management's projections

The Unit's R&D expenses consist mainly of relevant employee wages, laboratory expenses, material consumption and other expenses.

In 2013, R&D expenses were 4,670 thousand Euros, which reflect a rate of 3.9% out of revenues. In 2014, R&D expenses were 4,761 thousand Euros, which reflect a rate of approximately 4% of revenues.

In order to determine the projected cost we have analyzed the fixed and variable elements of the R&D cost structure, including the change in cost as a result of change in expected revenue. In 2015, it was assumed R&D expense will be 4,894 thousand Euros, 3.9% of revenue, similar to 2014 rate. For the following years we assumed a gradual decrease to 3.8% of revenue. It was assumed in the long term R&D cost will increase according to the permanent growth rate.

Impairment Examination of Goodwill

Operating Profit

The following table presents the Unit's estimated operating profit according to our forecast, and the actual operating profit, for the years 2013-2014 (thousands EUR):

€000	2013	2014	2015	2016	2017	2018	2019	Terminal
Operating profit	13,991	13,505	15,183	16,793	18,237	19,489	20,782	22,117
Operating margin	*11.7%*	*11.3%*	*12.2%*	*13.0%*	*13.7%*	*14.3%*	*14.9%*	*15.4%*

Source: BDO analysis and Management's projections

As a result of the analysis described above, the Units' operating profit for the forecast years will range from 12.2% in 2015, to 15.4% in the terminal year.

Capital Expenditure and Depreciation

The following table presents our capital expenditure expenses and depreciation forecast and the actual depreciation and capital expenditure expenses results for the years 2013-2014 (thousands EUR):

€000	2013	2014	2015	2016	2017	2018	2019	Terminal
Depreciation	3,029	3,008	2,776	3,004	3,021	3,035	3,049	3,064
% of revenue	*2.5%*	*2.5%*	*2.2%*	*2.3%*	*2.3%*	*2.2%*	*2.2%*	*2.1%*
Capital expenditure	(1,600)	(1,594)	(1,600)	(1,953)	(2,115)	(2,428)	(2,744)	(3,064)
% of revenue	*1.3%*	*1.3%*	*1.3%*	*1.5%*	*1.6%*	*1.8%*	*2.0%*	*2.1%*

Source: BDO analysis and Management's projections

Depreciation expenses were about 3,008 thousand Euros in 2014. In order to forecast the depreciation expense projections it was assumed depreciation expense will increase slightly up to approximately 3,064 thousand Euros in the terminal year, to about 2.1% of revenue.

Forecast of capital expenditure expenses is based on management's policy regarding investment plans and in light of the investments required for the Unit's operations. We have examined the rate of investment (out of revenue), in 2013and 2014, and found the average rate is about 1.3% of revenue.

According to Management, in 2015, the investment will be 1,600 thousand Euros representing 1.3% of total revenues, to maintain the existing, and during the forecast years the investment will increase to a rate of about 2.1% of total revenue. It was assumed that, in the terminal year, the investment will be equal to the depreciation.

Impairment Examination of Goodwill

Working Capital

The Unit's working capital forecast was calculated based on the Unit's historical data, as of the years 2012-2013, and additional information from Management.

Working capital days were estimated to be:

- **Trade receivables days** – 50 days;
- **Other receivables days** – 3 days;
- **Inventory days -** 110 days;
- **Trade payables days -** 50 days;
- **Other payables days -** 24 days.

Income Tax

The general requirements of IAS36 require that impairment tests are carried out exclusive of tax effects. Consequently, the discount rate used to estimate the present value of the cash flows should be calculated as a pre-tax discount rate. In order to estimate the pre-tax discount rate, present value was first calculated based on weighted average cost of capital. Then the suitable pre-tax discount rate was calculated according to the present value (see following pages).

In order to calculate the pre-tax discount rate, we used a tax rate of 29%, which is the effective tax rate for the Unit (Management information, based on tax rates in countries in which the Unit operates). We note we added to the enterprise value a tax shield, received from Management. The tax shield's value derives from potential tax savings. These tax savings reflect the future tax benefits associated with amortizing the asset for income tax purposes. We note the related amortisation costs are not included in the cash flows.

Impairment Examination of Goodwill

Discount rate (WACC)

The general requirements of IAS36 require that impairment tests are carried out exclusive of tax effects. Consequently, the discount rate used to estimate the present value of the cash flows should be calculated as a pre tax discount rate. When applying the Income Approach, the cash flows expected to be generated by a business are discounted to their present value equivalent using a rate of return that reflects the relative risk of the investment, as well as the time value of money. This return, known as the weighted average cost of capital ("**WACC**") is calculated by weighting the required returns on interest-bearing debt and common equity capital in proportion to their estimated percentages in an expected industry capital structure.

The general formula for calculating the WACC is:

WACC = Kd (D%) + Ke (E%)

WACC=	Weighted average rate of return on invested capital;
Kd=	After-tax rate of return on debt capital;
D%=	Debt capital as a percentage of the sum of the debt, preferred and common equity capital ("Total Invested Capital");
Ke=	Rate of return on common equity capital; and
E%=	Common equity capital as a percentage of the Total Invested Capital.

Discount rate (WACC)

CAPM has been empirically tested and is widely accepted for the purpose of estimating a company's required return on capital. In applying the CAPM, the rate of return on capital is estimated as the current risk-free rate of return, plus a market risk premium expected over the risk-free rate of return, multiplied by the "**beta**" for the valued company. Beta is defined as a risk measure that reflects the sensitivity of a company's stock (**or capital**) price to the movements of the stock market as a whole.

The CAPM rate of return on capital is calculated using the formula:

Ke **=** Rf + β(Rm * Rf)+ SCP+ Sp **Where**;

Ke=	Rate of return on capital (in this case, Total Invested Capital);
Rf=	Risk free rate of return; (in this case, the interest taken is index-linked bond yield for the period of 10 years, weighted, Germany, UK, and Italy); (Source: Bloomberg)

Impairment Examination of Goodwill

Discount rate (WACC)

B=	Coefficient of relative risk (B) - The relative risk coefficient. This factor reflects the relative risks involved in a specific investment and is based on the correlation between the return on investment with a return on the capital market as a whole. When the coefficient is greater than 1, business is highly sensitive to changes in market conditions (ie, in the case a recession the sector will be worse off than other sectors, and in the case of an economic boom the sector will be better off than other industries). When the coefficient is smaller than 1, the value of the average business is less sensitive to changes in market conditions. Beta of operations was calculated in accordance with Frutarom's. In order to calculate the ß of Savory, we relied on the comparable companies, operating in the sector of production of flavor and fragrance raw, such as: Frutarom, IFF, Givaudan, Symrise. In addition, we neutralized the financial leverage from ß of each company and averaged the non-leveraged ßs and added the specific financial leverage of the company. The ß is estimated to be approximately 0.77. For purposes of calculation, the Beta was calculated over a 5 year weekly period**.**
Rm–Rf=	The market risk premium is the weighted average of the risk premium of the German, Italian, English markets and is estimated to be 6.71% (Source: Damodaran 2014 - NYU Business School).
SCP	Small cap premium- Investment in small companies carry greater risk than investing in large, established companies. Therefore investors expect a higher return when they invest in small companies. Premium=6.01%..- Ibbotson valuation edition 2013 yearbook;
Srp	Specific Premium.

Discount rate (WACC)

Weights of debt and equity, taking into account in the WACC calculation are the average outstanding debt and equity weights of comparable companies.

After-tax discount rate of the cash-generating unit is determined was based on WACC model and on the following parameters:

Parameter	Symbol	Value	Source
Unit's Debt	D/(D+E)	8.9%	Based on comparable companies analysis
Unit's Equity	E/(D+E)	91.1%	Based on comparable companies analysis
EV	V	**100%**	
Cost Of Debt	Kd	1.20%	The Company's Cost of Debt
Tax Rate	T	29.0%	Effective tax rate of the unit
Beta	ß	0.77	Levered Beta - According to comparable companies
Risk Free Rate	Rf	0.86%	תשואת אג"ח צמודות מדד ל-10 שנים (מקור: מערכת בלומברג)
Market Premium	Rm-Rf	6.71%	Weighted Italy & Germany & United Kingdom market risk premium (Damodaran 2014)
SCP	SCP	6.01%	Ibbotson
Cost Of Capital	Ke	12.01%	Rf +ß*(Rm-Rf)+SCP+SRP
Weighted average cost of capital	**WACC**	**11.00%**	D*(1-T)*Kd+E*Ke

Source: BDO analysis.

The discount rate represented above reflects an after-tax discount rate; we have adapted it to reflect a pre-tax discount rate. The after tax discount rate is 11% while we believe that the pre-tax discount rate is approximately 14.6%.

Terminal growth rate

The terminal growth rate of 2.5% was determined based upon the real economy expected growth rate in the long term.

Impairment Examination of Goodwill

The Unit's Cash Flow

Based on the assessments above, below is the cash flow projections of 2015-2019 and actual 2013-2014 (thousands EUR):

€000	2013	2014	2015	2016	2017	2018	2019	Terminal
Revenue	120,020	120,004	124,805	129,173	133,048	136,374	139,784	143,278
Growth rate	*8.0%*	*0.0%*	*4.0%*	*3.5%*	*3.0%*	*2.5%*	*2.5%*	*2.5%*
Total cost of sales	80,616	80,634	83,036	85,146	87,007	88,596	90,218	91,875
% of revenue	*67.2%*	*67.2%*	*66.5%*	*65.9%*	*65.4%*	*65.0%*	*64.5%*	*64.1%*
Gross profit	**39,404**	**39,371**	**41,769**	**44,027**	**46,041**	**47,778**	**49,565**	**51,404**
Gross margin	*32.8%*	*32.8%*	*33.5%*	*34.1%*	*34.6%*	*35.0%*	*35.5%*	*35.9%*
Operating expenses								
R&D	4,670	4,761	4,894	5,014	5,120	5,210	5,301	5,394
% of revenue	*3.9%*	*4.0%*	*3.9%*	*3.9%*	*3.8%*	*3.8%*	*3.8%*	*3.8%*
S&M	13,786	14,652	15,110	15,523	15,888	16,198	16,515	16,838
% of revenue	*11.5%*	*12.2%*	*12.1%*	*12.0%*	*11.9%*	*11.9%*	*11.8%*	*11.8%*
G&A	6,957	6,453	6,581	6,696	6,796	6,881	6,967	7,055
% of revenue	*5.8%*	*5.4%*	*5.3%*	*5.2%*	*5.1%*	*5.0%*	*5.0%*	*4.9%*
Total operating expenses	**25,412**	**25,866**	**26,586**	**27,234**	**27,804**	**28,289**	**28,784**	**29,287**
% of revenue	*21.2%*	*21.6%*	*21.3%*	*21.1%*	*20.9%*	*20.7%*	*20.6%*	*20.4%*
Pre tax operating profit	**13,991**	**13,505**	**15,183**	**16,793**	**18,237**	**19,489**	**20,782**	**22,117**
Pre tax operating margin	*11.7%*	*11.3%*	*12.2%*	*13.0%*	*13.7%*	*14.3%*	*14.9%*	*15.4%*
Adjustments								
Change in working capital			(2,935)	(831)	(736)	(631)	(646)	(662)
Depreciation			2,776	3,004	3,021	3,035	3,049	3,064
Capital expenditure			(1,600)	(1,953)	(2,115)	(2,428)	(2,744)	(3,064)
Net cash flow from operating activities			**13,424**	**17,014**	**18,408**	**19,465**	**20,440**	**21,455**
Discounted Cash Flow			**12,538**	**13,863**	**13,084**	**12,070**	**11,057**	**95,676**

:

Source: BDO analysis and financial statements

Impairment Examination of Goodwill

CGU's Value in use

Below represents the value of the CGU's operations by the value in use method:

€000	
Current value 2015-2019	62,612
Current terminal value	95,676
Total value of the activity	**158,289**

Sensitivity Analysis

The following table provides a sensitivity analysis of the recoverable amount with respect to a pre-tax discount rate and the terminal growth rate (thousands EUR):

		Pre tax discount rate				
		12.6%	*13.6%*	*14.6%*	*15.6%*	*16.6%*
Growth rate	*1.5%*	178,229	163,485	151,002	140,298	131,021
	2.0%	183,537	167,764	154,501	143,196	133,446
	2.5%	189,370	172,427	**158,289**	146,314	136,043
	3.0%	195,809	177,529	162,402	149,679	138,830
	3.5%	202,952	183,134	166,885	153,321	141,829

Section 5

Comparison of Recoverable Amount and Book Value

Comparison of Recoverable Amount and Book Value

CGU's Book Value

After finding the recoverable amount of the activity, as mentioned before above, we compare it to the book value of operations.

If the recoverable amount of the asset is less than the carrying amount, then the entity it is required to perform an estimation of the impairment of the asset being examined and reduce it accordingly.

In favor of finding the carrying amount of activity and goodwill associated, we examined the balance sheet data as of December 31, 2014 (thousands EUR):

€000	2014
Accounts receivable	16,200
Other receivable	813
Inventory	19,945
Net Fixed Assets	18,537
Software	1,414
Total operational assets	**56,909**
Accounts payable	(8,484)
Other short-term liabilities	(5,536)
Other payables, related parties	(3,831)
Pension Liability	(3,411)
Total operational liabilities	**(21,262)**
Customer relations and know How, Gross	15,062
Deferred tax (PPA)	(4,084)
Goodwill	78,609
Sub total	**89,587**
Total carrying amount	**125,234**

Source: Management information

The

To observe potential impairment, the assets recoverable amount was compared to the carrying amount.

Difference calculated between the new value of the activity and the fair value of identifiable assets and liabilities will be the new goodwill. The difference between the values of goodwill is the impairment loss on goodwill.

The following table summarizes the results of the impairment examination for the Unit, under IAS 36:

€000	2014
Recoverable amount	158,289
Carrying amount	125,234
Impairment amount	–

Source: BDO analysis.

The analysis of the table above shows that the recoverable amount of the Unit is greater than its carrying amount, as of the Valuation Date. Therefore, Frutarom's savory Division goodwill is not deemed to be impaired.

Valuation

US Operations
As Of December 31, 2014

Frutarom Industries Ltd.

Impairment Study – US Operations

As Of December 31, 2014

BDO Ziv Haft
Amot Bituach House Building B, 48
Menachem Begin Road, Tel Aviv
66180
Israel

Dear Sirs,

We were requested by Frutarom Industries Ltd. (Hereinafter: **“Frutarom”** or the **“Company"**) to perform an Impairment Examination Study (Hereinafter: the **“Study”**) of the United States Flavor operations sector (Hereinafter: the "**flavor operations**" or the “**Unit"**) for December 31, 2014 (hereinafter: **"valuation date")** under the requirements of Statement of International Accounting Standards 36 (**IAS 36**). To the best of our knowledge there is no prevention, legal or other, to perform the Study enclosed herein.

Our findings will be used by Frutarom, its management and its critics, and that financial reporting purposes as part of the accounting principles and financial reporting practices in Israel and required by law, including in accordance with IAS 36 Impairment of Assets (IAS 36). This work is intended for the exclusive use of Frutarom, its management, independent critics only by law.

Based on our study, we have concluded that the Unit's Goodwill is not deemed to be impaired, as of December 31, 2013.

We know that this examination will be used and / or be included in the financial statements as stated in the regulations under the Securities Law - 1968. No other use of this opinion except for the above, including, quoted in full or parts of it, and can be transferred to third parties some, without the express written approval in advance.

In the course of our Annual Goodwill Impairment Test, we relied upon financial and other information, including prospective financial information obtained from Management and from various public, financial and industry sources. Our conclusion is dependent on such information being complete and accurate in all material respects.

This examination does not represent due diligence and does not purport to include the information, tests and exams or any other information included in due diligence.

We did not check the information independently, except for the fairness examination.

We performed a number of examinations:

• Analyzed business results of operations in recent years, making a fairness examination of revenue and expenditure forecasts used in this document;

• An examination of the expenses of operations;

• Review of operating profitability of operations.

Economic opinion is not an exact science, and should reflect a reasonable and fair condition as of a particular time, on the basis of known data, assumptions and forecasts that were determined. Changes in the factors and / or information, may change the underlying basic assumptions and in accordance with the conclusions. The calculations in this study were performed using a spreadsheet, so there may be rounding differences.

We wish to note that we have no personal interest in the Company, we are independent of the Company or one of the Group as such term is defined in the auditors 1955 and the regulations promulgated thereunder. Also note that are no conditions for legal fees in connection with the results of this opinion.

For our work, we relied on data and documents, as follows:

- Pro-forma reports of US operations for 2012-2014;
- Forecasts for the years 2015-2019 operations;
- Financial and operational business information obtained from Frutarom's management;
- Barnea reports of Frutarom 2013;
- Financial and operational business information, which was obtained by Frutarom's management;
- Information regarding the Company's operations in the United States;
- Conversations with the Company's management;
- Public data.

Based on our work and the findings set out in our general conclusion that the value of goodwill activity appears in the books did not decrease, and therefore does not require re-estimation and reduction of intangible assets of operations as shown below:

$000	
Current value 2015-2019	73,718
Current terminal value	115,018
Total value of the activity	**188,736**

Only authorized personnel should have access to this document, any person who is not an official recipient of this report or who signed a letter of personal responsibility to BDO Consulting Group is not authorized to access this document. BDO is not responsible for unauthorized persons seeing this document or any other person obtaining this document. If an unauthorized person chooses to rely on the contents of this document, that person is solely responsible. Unauthorized person, who reads this document is required understand the following conditions:

• This document was prepared in coordination with the guidelines, provided by the recipient exclusively for personal use.

• BDO Consulting Group, its partners, employees and agents have no responsibility towards the reader or any damage caused (including commitment, negligence or responsibility), or otherwise. We are not obliged to discuss the basis of this document or the accuracy of its contents and information since the date of composing it. We are not responsible from any loss, damage or expense that resulted from any readers who have chosen to use or rely on this document.

• Our work was directed in coordination with the appropriate professional instructions. In other sectors, the relevant procedures and work practices may display data differently. This document was not conducted in coordination with the procedures and practices of any professional body.

• Do not refer to this document or cite it or parts of it, exposed to any other third party.

In forming our opinion we have relied on sources, which appeared to us as reliable, and nothing came to our attention, which is likely to indicate the lack of reasonability of the data we used. We did not examine the data in an independent manner and, therefore, our work does not constitute verification of the correctness, completeness or accuracy of the data.

Details regarding the valuation specialist

BDO Consulting and Management Ltd. were founded by the partners of BDO Certified Public Accountants.
BDO Consulting and Management is part of the international BDO network, provides a full range of business services required for national and international businesses in any sector. Our Company has vast experience in the following fields: business valuations, financial and tax due diligence, goodwill and intangible assets valuations, financial analyses, business plans, project finance PFI/PPP advisory, M&A, investment banking and more.

Consulting & Management Ltd.

Respectfully submitted,

BDO Ziv Haft

Contents

Section 1
US Operations Overview

US Operations Overview

General

In 2011, Frutarom completed the acquisition of FSI (Cincinnati). During 2012, through the consolidation and merger of FSI operations with existing activities in the US' Frutarom operated to improve its flavors sector in North and Central America, while creating an operating base on the West Coast of the United States. Existing operating activities include, among other things, FSI (Corona) and the remaining of flavors and ingredients of the Company, throughout the United States. Most of the sales these operations are in the United States, and most of the customers are in the US.

While consolidating US operations, R&D systems, manufacturing, supply chain,, marketing and sales department of the US activities were merged, while maximizing synergies between them. In addition, Frutarom works to maximize the cross selling, deriving from consolidation of operations in the United States.

The flavor operations are located in Cincinnati, where the Company has a factory and R&D labs. The new plant's construction was completed in 2012, with the possibility of expanding into other activities and activities in which the Company is not yet engaged in.

On December 11, 2013, Frutarom signed an agreement to acquire 100% of the shares of an American Company, Hagelin & Company Inc. (hereinafter: "Hagelin"), in exchange for $52.4 million. The acquisition was completed on the date of signing. Hagelin is engaged in the development, manufacturing and marketing of flavors and unique flavor technologies for the food industry, with a focus on the vegetation of flavors for the beverage industry. Hagelin specializes, among other things, in the

General

development of advanced technologies with a focus on reducing salt, reducing sugar and calories all while improving the taste experience. Hagelin has a customer base that includes leading global and domestic food and beverage manufacturers in the US, UK and emerging markets, particularly in Central and South America and Africa, characterized by high growth rates.

Hagelin's English operations merged with Frutarom's UK operations and the US operation of Hagelin is at final stages of the consolidation process with Frutarom's US activity.

As mentioned before, the Company's flavor department develops and manufactures flavors. The Company has a complete production line of flavors, herbs, herbal extracts, dietary supplements and unique products for different industries around the world.

As part of its US operations, the Company produces flavors for food and beverages. Beverage flavours are used in carbonated, non carbonated, dairy and coffee beverages, flavored water, energy drinks, cocktails, wines, liqueurs, powdered drinks, protein powders, teas and other functional beverages, sold to the consumer. The increase in demand for natural products from consumers has led the Company to produce all of its products, using high quality raw materials, while maintaining repeated laboratory tests and supervision of existing products.

US Operations Overview

Products

Listed below are the Company's US operations range of products:

Natural flavours and "natural & artificial" high quality flavours, - These products include: Emulsions, flavour concentrates, dry concentrate flavours, flavouring for carbonated, non-carbonated, and functional beverages, dairy products, coffee, tea and herbal tea, pastries, snacks, ice creams and desserts, savory products, sweets, vegetables and spices.

Botanical Products- These products include: liquid extracts and powders (which are included custom and standard mixtures), herbal powders and herbal teas.

Powder Blends - These products include: instant drinks, milk mixtures, coffee and tea products, protein-based drinks and energy drinks.

Specialty Products – These are custom-made products engineered for the client. Major manufacturing facilities of the Company allow it to blend/mix colors, vitamins, minerals, herbal-based products and proteins. This allows the Company to accelerate the process of production, their production facilities customers to.

US Operations Overview

Description of US operations

The following table represents balance sheet of US operations, as of December 31, 2014 (thousands of USD):

$000	31.12.2014
Current Assets	
Cash & cash equivalents	2,636
Accounts receivable	7,148
Related Parties	2,007
Other receivable	2,976
Inventory	7,326
Total current assets	**22,093**
Long-term assets	
Net fixed assets	13,691
Other assets, net	95,799
Total long-term assets	**109,490**
Total assets	**131,583**
Current liabilities	
Short-term credit	7,555
Accounts payable	4,080
Related Parties	6,121
Accrued expenses	2,175
Total current liabilities	**19,931**
Long term liabilities	
Long-term credit	36,621
Pension liability	422
Long-term loans to related parties	42,473
Deferred tax	2,927
Total long term liabilities	**82,443**
Total liabilities	**102,374**
Total shareholder's equity	29,209
Total liabilities and equity	**131,583**

Source: unaudited consolidated statements received from Frutarom's management based on the audited financial statements of operations.

he following profit and loss statements of the US flavors operations for 2014 and a 2013 pro forma statement (thousands of USD):

$000	2013	2014
Revenue	65,850	70,272
Growth rate	*.ל.ר*	*7%*
Cost of sales	33,471	37,048
% of revenue	*51%*	*53%*
Gross profit	**32,379**	**33,224**
Gross margin	*49%*	*47%*
S&M	7,187	5,767
% of revenue	*11%*	*8%*
R&D	5,896	5,632
% of revenue	*9%*	*8%*
G&A	5,827	4,765
% of revenue	*9%*	*7%*
Operating profit	**13,469**	**17,060**
Operating margin	*20%*	*24%*

Source: unaudited consolidated statements received from Frutarom's management based on the audited financial statements of operations.

Section 2
Market Overview

Market Overview

Flavor and fragrance industry worldwide

The global market for flavors, fragrances and raw materials in 2012, was estimated at approximately $23 billion. Frutarom is not active in the fragrances market, but is active in the market of natural functional food ingredients (excluding the above estimate), and therefore, it believes to sell in the markets where it operates, approximately $18.5 billion. According to Leffingwell & Associates, Frutarom is ranked as one of the ten largest companies in the taste and smell markets.

In 2012, the research Company IAL Consultants, estimated that sales in industrialized countries (USA and Western Europe) in the flavors markets, in which the Company operates, will grow at an annual rate of 2%, from 2012 to 2017. Frutarom estimates that sales of raw materials, in those markets, will grow at an annual rate, similar to the years 2015 to 2017. According to these estimates, the growth rate in emerging markets where the Company operates, such as Asia, Central and South America, Eastern Europe and Africa, is expected to be significantly higher due to changes in consumer preferences in these markets and the transition to processed food, and can reach average annual rates of 5.9% from 2012 to 2017.

The manufacturers of the flavor, fragrance and fine ingredient markets can be divided into three main groups: large multinational companies; mid-sized companies; and local and small companies.

Flavor and fragrance industry worldwide

Large multinational manufacturers generally operate globally and have revenues in excess of $ 1 billion. In the global flavor and fragrance markets there are five such manufacturers which, according to Leffingwell & Associates, represent approximately 60% sales in the flavor, fragrance and fine ingredients markets (excluding sales of natural functional food ingredients and pharmaceutical/nutraceutical extracts). These multinational manufacturers focus primarily on customers who are large multinational food and beverage producers.

Local and small companies generally have revenues of less than $ 100 million (most of them are much smaller and sell only several million dollars). The Company estimates that in the global flavor and fragrance markets, there are approximately 500 such companies that, according to the estimation of Leffingwell & Associates, represent approximately 10% of the value of the flavor, fragrance and fine ingredients market (again excluding sales of natural functional food ingredients and pharmaceutical/nutraceutical extracts). These companies generally focus on smaller local customers and have limited capabilities in the areas of service, research and development and innovation.

Mid-sized companies, such as Frutarom, have revenues between $ 100 million and $1 billion. In the global flavor and fragrance markets there are only eight such mid-sized companies. According to the estimation of Leffingwell & Associates these eight companies represent approximately 30% of the value of the flavor, fragrance and fine ingredients market (excluding sales of natural functional food ingredients and pharmaceutical/nutraceutical extracts). Some of these mid-sized players focus heavily on specific geographic markets (such as the USA, France and Japan).

Market Overview

Flavors market

Flavors are the key building blocks that impart taste in processed food and beverage products and, as such, play a significant role in determining the consumer acceptance of the end products in which they are used.

The research Company IAL Consultant, estimates that global 2012 sales of flavors for the industry amounted to approximately US $ 8.7 billion. Flavor products are sold primarily to producers of prepared food, beverage, dairy, bakery, meat and fish, confectionery and pharmaceutical products.

The following are examples of end user products using flavors:

- **Beverages** - carbonated, noncarbonated, sport and functional, alcoholic and juices.
- **Dairy** - yogurt, drinking yogurt, ice cream, cheese and chilled desserts.
- **Bakery** - cakes and cookies, crackers and cereals.
- **Confectionery** - candy, chocolate, jam and chewing gum.
- **Savory and convenience food** - ready meals, instant soup, ready sauces and instant noodles.
- **Snacks** - potato chips and other savory snacks.
- **Meat** - sausages and frankfurters.
- **Processed Fish**.
- **Oral hygiene and pharmaceuticals** - toothpaste, mouthwash, vitamins and medicines.
- **Others** - animal feed and pet food and tobacco**.**

The global market for flavors has expanded rapidly over the last 60 years, primarily as a result of an increase in demand for, as well as an increase in the variety of, consumer end products containing flavors. The demand for consumer goods containing flavor products has increased as a result of rapid population growth and consumer preferences resulting from various factors such as increases in personal income, leisure time, health concerns and urbanization**.**

Market Overview

Flavors market

These factors have led to an overall increase in food and beverage products containing flavors and to rapid growth in demand for convenience food and foods with healthier and more natural content.

The following table sets forth the sales of flavours in 2012 and the projected annual growth rate in these geographic regions:

Country	World consumption in 2012 ($ million)	Average growth is expected in 2012-2017	Market share
Western Europe	1,712	1.30%	19.75%
Eastern Europe	585	2.70%	6.75%
North America	2,470	2.40%	28.49%
South America	651	7.60%	7.51%
Asia	2,652	6.20%	30.59%
Middle East and Africa	599	5.30%	6.91%
Total	**8,669**	**4.10%**	**100.00%**

According to the estimates above, the largest flavor market in 2012 was the Asian market representing approximately 30.6% of the global market, followed by North America with approximately 28.5%. The South American market had the most significant expected growth rate (7.6%) followed by the Asian market with estimated annual growth rate of about 6.2% in 2012-2017.

Flavors market - Characteristics

The following are the characteristics of the Flavor Market:

- **Reliable with high levels of service** - Food and beverage producers, the principal customers of flavor manufacturers, expect reliable, high-quality service to meet their needs in terms of support and lead time, while maintaining high quality, regulatory and safety standards. These requirements encourage the formation of long-term relationships between flavor producers and their customers. As a result, large multinational customers, and increasingly also mid-sized customers, have pruned the flavor suppliers that they will work with, placing those that remain on "core lists" creating a barrier to entry for small flavor manufacturers.

- **Research and development** - The development of flavor products in general and of new flavor extracts in particular is a complex, creative and technological process that calls for depth of knowledge and skill on the part of a flavor manufacturer's research and development personnel. Effective research and development is critical in ensuring a continuous stream of innovative products and in maintaining the profitability and growth of a flavor manufacturer. The initiative for the development of new flavor products can be spurred by the flavor manufacturer or by the customer who is in need of a specific flavor for use in a newly developed end product. As such, in order to anticipate market demands, a flavor manufacturer's research and development personnel are required to be familiar with the taste requirements of various end product types and target markets. In addition, as most flavors are tailor made for a specific customer, a close collaborative relationship with the customer is essential. These flavor formulas are treated as commercial secrets and remain the proprietary asset of the flavor manufacturer.

Market Overview

Flavors market - Characteristics

As most flavor products are tailor-made for a customer, customers are less likely to replace suppliers for such flavor products during the course of the end products' life cycle.

- **Low price sensitivity** - Since flavor products play a major role in determining the flavor of the end product to which they contribute, they are a vital element of its success. Flavor products cannot be precisely matched and their cost, compared to the total cost of the end products, is negligible. When selecting a flavor supplier, a customer will generally place a greater emphasis on the reputation, innovation, service, quality and consistency of the supplier than on the price of its flavors. The demand for flavors is therefore generally less sensitive to changes in price.
- **Production processes** - Flavor products in general and flavors in particular typically contain a variety of ingredients (typically over 30 per flavor), which are blended using unique formulas created by a manufacturer's flavor expert. The production processes involved in the manufacture of flavor products are less complex and capital intensive compared to those of fine ingredients. However, the production process for flavor products requires skill and knowhow to achieve the required consistency and quality.
- **High and relatively stable profitability** - As the flavors market tends to be characterized by long-term relationships and high customer loyalty, combined with relatively low price sensitivity and simple production processes, it generally benefits from high and stable margins. This is true also in comparison to the fine ingredient industry.

Flavors market - Characteristics

Flavors are sold primarily to food and beverage producers; therefore the flavor market is generally driven by trends characterizing the demands of food and beverage consumers.

According to Data Monitor, global sales in the food and beverage market amounted to $4,650 billion in 2012. Frutarom estimates that over 60% of such total global sales are generated by mid-sized, local and small food and beverage producers. Although there has been a general trend towards consolidation in the food and beverage industry, Frutarom estimates that mid-sized (annual revenues of between $100 million and $1 billion) and local and small (annual revenues of below $100 million) food and beverage producers will continue to play a significant role in the market, and that new mid-sized, local and small producers will continue to emerge.

Large multinational flavor manufacturers often focus on large multinational food and beverage producers, offering their customers a high level of service and tailor-made product development. Frutarom believes that these flavors producers focus to a lesser extent on mid- sized and local customers, offering limited service and offering less customizable product offering to these customers.

Market Overview

Food and Beverage Market - Characteristics

However, the Company believes that mid-sized and local food and beverage producers require the same level of service and tailor-made products as their larger counterparts, and also require short lead times and manufacturing flexibility. Small, localized flavor producers generally do not have the product variety and service capabilities to support the needs of these customers. A specific example of this type of customer is the private label customer. This situation creates a business opportunity for mid-sized flavor producers to service this segment.

Food and Beverage Market - Tendencies

The following are the main trends in the consumer market for food and beverages which in turn drive the flavor market:

Local and global tastes - Taste preferences vary by geographic location and among different cultures. Flavor manufacturers must have thorough knowledge of local tastes in each of the countries in which they are active. It is also important for a global flavor manufacturer to have a physical presence in its key target markets in order to facilitate direct contact with customers, to better understand local tastes and to be able to respond quickly and efficiently to changes in consumer preferences. Additionally, the trend toward globalization now characterizes the flavor industry as multinational food and beverage customers are now launching global brands in many different markets simultaneously, often by changing the taste profile to meet the preferences of the respective populations worldwide.

Food and Beverage Market - Tendencies

- **Preference of natural products** - There has been a general increase in consumer demand for food and beverage products containing natural ingredients and having dietary values (reducing fat, salt, cholesterol, etc.). Natural products are generally perceived by consumers as being of higher quality, healthier and more environmentally friendly. Similarly, there is growing demand for organic products and 'clean label' products. As a result, natural food and beverage products are viewed as specialty, premium products that can command higher prices. This trend has created new opportunities for flavors manufacturers to develop new and innovative natural flavor products.

- **Continuously growing consumption of convenience food** - There is an increase in demand for processed foods with greater convenience (consumed both inside and outside of the home). This increase in demand for convenience foods has been spurred by new packaging and cooking technologies as well as changing social habits and consumer preferences. Examples of convenience foods include "ready to eat" meals, fresh pasta; ready-to-cook, fresh seasoned or marinated meat or poultry; salads; and sauces in liquid form. This has created new opportunities for flavor manufacturers in the savory flavors and functional fine ingredients fields which are responsible for the creation of food texture and its extended shelf life, to develop and market flavors and unique fine ingredients products for this segment.

Market Overview

Food and Beverage Market - Tendencies

- **Private label** - private label goods manufacturers, which tend to be mid-sized, local or small food manufacturers, are a growing customer segment in the flavor industry. Over the last decade consumers of food products have become increasingly price conscious, increasing sales of private label products in comparison to the branded food and beverage industry. This trend was accelerated in 2009 as a result of the economic crisis. As a result, supermarket chains and other retailers have been increasing their private label product offerings.

- **Emerging markets** - In recent years, certain developing markets, such as Asia, Central and South America, Eastern Europe and Africa have experienced above-market-average growth in demand for flavors products. Further, these markets have been characterized by a trend towards increased consumption of processed foods, which in turn has driven the emergence of mid-sized, local and small food companies, creating new market opportunities for flavor manufacturers.

Food and Beverage Market - Critical Success Factors

The critical success factors in the flavor segment are:

- **Long-term relationships** - Long-term relationships with customers and collaboration in the development of new products.

- **Global and local presence in target markets** - Knowledge of the various flavor preferences in the different markets and the ability to provide global and local support to customers.

- **Superior and reliable service** - The ability to provide a high level of service and the reliability of a flavors manufacturer in giving service are critical for mid-sized, local customers and multinational customers.

- **Presence in emerging markets** - Emerging markets grow at considerably higher rates in comparison to developed markets. Presence in these key areas, along with knowledge and understanding of their unique needs and the ability to provide support to local manufacturers is a critical success factor.

- **Innovation in research and development** - The ability to develop innovative products both at the initiative of the flavor manufacturer and in collaboration with customers is of extreme importance.

- **Compliance with strict quality, regulatory and safety standards** - Since the flavors are intended principally for the food and beverage and pharmaceutical markets, they must comply with strict quality, regulatory and safety standards

Market Overview

Food and beverage market - Critical Success Factors

- Procurement of raw materials –there is a growing importance in diverting resources to targeted procurement in countries that are an important source of raw materials, such as China, India and Brazil, while expanding the pool of suppliers, reducing costs through an efficient global procurement network and strengthening relationships with producers, processors and growers of raw materials, will provide a secure and reliable supply and improve procurement costs..

Flavors Market - Competition

In the flavor market, Frutarom's main competitors consist of large global manufacturers, mid-sized companies and smaller, local manufacturers. Competition is based to a large extent on innovation, product quality, the ability to provide the customer with added value, and establish and maintain long term customer relationships, value added service, reliability and development of products which are tailor made for the customers' needs and the future market directions. As the cost of flavors accounts for only a small percentage of the total cost of an end product, this market tends to display low price sensitivity. Flavor manufacturers must differentiate themselves by maintaining close collaborative relationships with customers, thorough knowledge and understanding of target markets, innovative abilities, effective research and development and an established reputation for consistent, reliable and effective service, product supply and quality, and the ability to supply product on short notice and with short lead time.

Flavors Market - Competition

Large multinational flavor manufacturers are established, experienced companies with a global presence and established technical and commercial capabilities, focusing primarily on large multinationals customers. The large multinational flavors producers with whom Frutarom competes include Givaudan, Firmenich, IFF Inc., Symrise and Takasago.

The midsized flavors manufacturers with whom Frutarom competes, focus on both large multinational food and beverage producers as well as and mostly on mid-sized and smaller food and beverage producers who tend to operate in smaller geographical regions. Mid-sized flavor manufacturers with whom Frutarom competes include Sensient, Mane, Robertet, Kerry Ingredients, Wild and Dohler.

The Company estimates that there are approximately 700 small and local flavor manufacturers with more limited research and development capabilities who focus on narrow market segments and local customers. In recent years there has been a trend towards consolidation in the flavor manufacturing industry, resulting in increasing market concentration.

Market Overview

Risks Factors

The risks of the global market of flavors, fragrances and fine ingredients refer to macroeconomic risks and to risks related to the Industry.

Risks Factors - Macroeconomic Risks-

The following are the main macroeconomic risk factors:

- **The effect of the global economy on the Company's activities** - Due to the nature of its global activity, Frutarom is exposed to fluctuations in the global economy. Economic crisis and recession in important target countries may cause dips in demand for the Company's products (mainly for premium products) and significantly slow down the development and launch of new products by the customers.

- **Stability in emerging markets** - Companies who operates in a number of countries outside of Western Europe and the United States, such as Russia, Turkey, Kazakhstan, Ukraine and China, is generally exposed to the political, economic and legal systems and conditions in these countries which are generally less predictable than in developed countries

Risks Factors - Macroeconomic Risks

- **Currency fluctuations** - The Company has sales, expenses, assets and liabilities denominated in currencies other than the U.S. due to that fact, fluctuations in the exchange rates of these foreign currencies could have an impact on a Company's results of operations.

- **Changes in interest rates** - The Company's sources of banking finance, as needed, for short and long term, are linked to different coins, according to the activity currency of the subsidiary, and bear Libor interest at variable rates in accordance with its policy. Therefore, if interest rates increase, the Company may not be able to refinance its credit agreements, or any other indebtedness, on attractive terms. Increases in interest rates will impact the Company's cash flow.

Market Overview

Risks Factors - Industry Risks

- **Extensive competition -** Companies in the global market of flavors, fragrances and fine Ingredients face increased competition both from large multinational and mid-sized companies as well as smaller local companies in many of the markets in which they operates. Some of the competitors have greater financial and technological resources, large sales and marketing organizations and great name recognition, and may therefore be better able to adapt to changes and trends in the industry. The global market for flavors is characterized by close, collaborative relationships between flavor manufacturers and their customers, particularly in the large multinational customer segment.

- **Changes in regulations -** Companies are subject to a variety of health, safety and environmental rules at national, state and local levels in the various countries in which it operates. Generally, there is a trend towards increased regulation in the industry in which the Group operates. This has been a result of increased public sensitivity toward the composition and use of flavor products and from the fact that as a result of their medicinal qualities and claimed health benefits, nutraceutical and functional food products are being increasingly viewed by regulators as having similar characteristics to pharmaceutical products, which may lead their subject to the regulatory framework governing the market for pharmaceutical products.

Risks Factors - Industry Risks

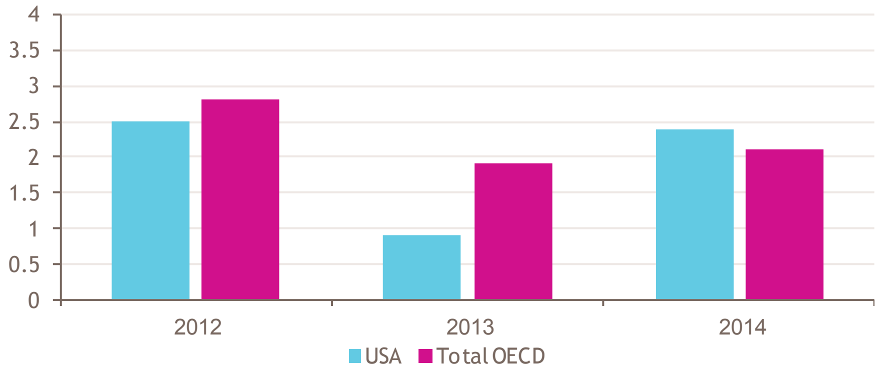
- **Environmental, health and safety regulations** - Companies in the flavor and fine ingredients industry also use, manufacture, sell and distribute a number of environmentally hazardous materials, and therefore are subject to extensive regulation regarding the storage, handling, manufacture, transportation, use and disposal of their products, ingredients and byproducts. Any increase in the stringency of applicable environmental regulations could have a material adverse effect on companies business, results of operations or financial condition.

Fluctuations in prices of raw materials - The last few years were characterized by relatively high fluctuations in the prices of raw materials used by companies in the flavor and fine ingredients industry, to manufacture its products. The global increase in demand for raw materials in general, and raw materials for the food industry, in particular, continues and strengthens in recent years. Source of the increase in demand is mainly in third world countries, which populations rapidly change their consumption habits. In addition, the raw materials market is affected by the food industry, which, in recent years, experiences a decrease in supply, which comes from damage to crops in different countries, arising from extreme and prolonged drought and floods. The phenomenon of decrease in supply is exacerbated by the increasing diversion of crops, such as wheat and soybeans, for corn and other crops which are sugar producers, which are now used to create ethanol and other materials which produce Bio Diesel.

Market Overview

Risks Factors - Industry Risks

Increased demand with supply reduction is usually translated into an increase in commodity prices. The following graph shows the rates of increase in food prices, as presented by the OECD, between the years 2012-2014:



Section 3
Methodology

Methodology

IAS 36 - General

The International Accounting Standard 36 Impairment of Assets (hereinafter "IAS 36") objective is to prescribe the procedures that an entity applies to ensure that its assets are carried at no more than their recoverable amount. An asset is carried at more than its recoverable amount if its carrying amount exceeds the amount to be recovered through use or sale of the asset. If this is the case, the asset is described as impaired and the Standard requires the entity to recognize an impairment loss. The Standard also specifies when an entity should reverse an impairment loss and prescribes disclosures.

This Standard shall be applied in accounting for the impairment of all assets (other than exceptions as they appear in the standard content) or cash generating unit(s) including goodwill acquired from business combination. Goodwill acquired in business combination represents the value of the intangible assets which cannot be separately identified or separately recognized. Goodwill does not generate cash flow independently from other cash-generating unit(s), and often contributes to the cash flows of several cash-generating units. The Standard requires goodwill acquired in a business combination to be tested for impairment as part of impairment testing of the cash-generating unit(s) to which it relates, once a year or when there is a sign of impairment loss.

Definitions

The following terms are used in this Standard with the meanings specified:

Carrying amount is the amount at which an asset is recognized after deducting any accumulated depreciation (amortization) and accumulated impairment losses thereon.

A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are independent of the cash inflows from other assets or groups of assets.

Corporate assets are assets other than goodwill that contribute to the future cash flows of both the cash-generating unit under review and other cash-generating units.

Depreciation (Amortization) is the systematic allocation of the depreciable amount of an asset over its useful life. (In the case of an intangible asset, the term ‘amortization’ is generally used instead of ‘depreciation’. The two terms have the same meaning).

Fair value less costs to sell is the amount obtainable from the sale of an asset or cash-generating unit in an arm’s length transaction between knowledgeable, willing parties, less the costs of disposal.

An impairment loss is the amount by which the carrying amount of an asset or a cash-generating unit exceeds its recoverable amount.

The recoverable amount of an asset or a cash-generating unit is the higher of its fair value less costs to sell and its value in use.

Methodology

Determining an Impairment Loss

An entity shall assess at each reporting date whether there is any indication of impairment of an asset. If any such indication exists, the entity shall estimate the recoverable amount of the asset.

Regardless of whether there is any indication of impairment, the entity shall also:

▪ Conduct an annual assessment of impairment of an intangible asset's indefinite useful life or an intangible asset that is not yet available for use by comparing the value to its recoverable amount.

▪ The annual assessment of impairment of goodwill acquired in a business combination.

The Standard defines number of steps for the identification, recognition and measurement of value loss of an asset or cash generating unit. Moving on to the next step is subjected to the fulfillment of the previous step.

Identifying an asset that may be impaired

An entity shall assess at each reporting date whether there is any indication that an asset may be impaired. In assessing whether there is any indication that an asset may be impaired, an entity shall consider, as a minimum, the following indications:

Determining an Impairment Loss

External sources of information:

- During the period, an asset's market value has declined significantly more than would be expected as a result of the passage of time or normal use.

  Significant changes with an adverse effect on the entity have taken place during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the entity operates or in the market to which an asset is dedicated.

- Market interest rates or other market rates of return on investments have increased during the period, and those increases are likely to affect the discount rate used in calculating an asset's value in use and decrease the asset's recoverable amount materially.

- The carrying amount of the net assets of the entity is more than its market capitalization.

Internal sources of information:

- Evidence is available of obsolescence or physical damage of an asset.

Methodology

Determining an Impairment Loss

- Significant changes with an adverse effect on the entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used. These changes include the asset becoming idle, plans to discontinue or restructure the operation to which an asset belongs, plans to dispose of an asset before the previously expected date, and reassessing the useful life of an asset as finite rather than indefinite.
- Evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected.

If any indication of value loss exists, the entity shall estimate the recoverable amount of the asset. In case the value of the recoverable amount found is lower than the respective Carrying amount, the entity shall depreciate the value of the asset or the Cash-generating unit accordingly.

The standard requires an intangible asset with an indefinite useful life or not yet available for use and goodwill to be tested for impairment, once a year, regardless to the existence of indication of value loss.

Measuring Recoverable Amount

The recoverable amount of an asset or a cash-generating unit is the higher of its fair value less costs to sell and its value in use.

The Standard prescribes that it is not always necessary to determine both an asset's

fair value less costs to sell and its value in use, where either of these amounts exceeds the asset's carrying amount.

Furthermore, the Standard points out that there are cases where it is not possible to determine fair value less costs to sell of an asset, particularly when the asset is not traded in an active market. In such case, the entity may use the asset's value in use as its recoverable amount.

Fair value less costs to sell

The best evidence of an asset's fair value less costs to sell is a price in a binding sell agreement in an arm's length transaction, adjusted for incremental costs that would be directly attributable to the disposal of the asset.

If there is no binding sell agreement but an asset is traded in an active market, fair value less costs to sell is the asset's market price less the costs of disposal.

If there is no binding sell agreement or active market for an asset, fair value less costs to sell is based on the best information available to reflect the amount that an entity could obtain, at the end of the reporting period, from the disposal of the asset in an arm's length transaction between knowledgeable, willing parties, after deducting the costs of disposal. In determining this amount, an entity considers the outcome of recent transactions for similar assets within the same industry.

Costs of disposal, other than those that have been recognized as liabilities, are deducted in determining fair value less costs to sell.

Methodology

Fair value less costs to sell, continued

Costs of disposal are incremental costs directly attributable to the disposal of an asset, such as legal costs and similar transaction fees, costs of removing the asset and direct incremental costs to bring an asset into condition for its sale (excluding finance costs and income tax expense).

Value in use

The following elements shall be reflected in the calculation of an asset's value in use:

- An estimate of the future cash flows the entity expects to derive from the asset;
- Expectations about possible variations in the amount or timing of those future cash flows;
- The time value of money, represented by the current market risk-free rate of interest;
- The price for bearing the uncertainty inherent in the asset; and
- Other factors, such as illiquidity, that market participants would reflect in pricing the future cash flows the entity expects to derive from the asset.

Estimating the value in use of an asset involves the following steps:

- Estimating the future cash inflows and outflows to be derived from continuing use of the asset and from its ultimate disposal; and
- Applying the appropriate discount rate to those future cash flows.

Measuring Recoverable Amount, continued

In measuring value in use an entity shall:

- Base cash flow projections on reasonable and supportable assumptions that represent management's best estimate of the range of economic conditions that will exist over the remaining useful life of the asset.
- Base cash flow projections on the most recent financial budgets/forecasts approved by management, but shall exclude any estimated future cash inflows or outflows expected to arise from future restructurings or from improving or enhancing the asset's performance. Projections based on these budgets/forecasts shall cover a maximum period of five years, unless a longer period can be justified.
- Estimate cash flow projections beyond the period covered by the most recent budgets/forecasts by extrapolating the projections based on the budgets/forecasts using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified. This growth rate shall not exceed the long-term average growth rate for the products, industries, or country or countries in which the entity operates, or for the market in which the asset is used, unless a higher rate can be justified.

When the carrying amount of an asset does not yet include all the cash outflows to be incurred before it is ready for use or sale, the estimate of future cash outflows includes an estimate of any further cash outflow that is expected to be incurred before the asset is ready for use or sale.

Methodology

Measuring Recoverable Amount, continued

Estimates of future cash flows shall not include estimated future cash inflows or outflows that are expected to arise from:

- A future restructuring to which an entity is not yet committed; or
- Improving or enhancing the asset's performance.
- Cash inflows or outflows from financing activities; or
- Income tax receipts or payments.

Future cash flows are estimated in the currency in which they will be generated and then discounted using a discount rate appropriate for that currency. An entity translates the present value using the spot exchange rate at the date of the value in use calculation

Discount rate

The discount rate shall be a pre-tax rate that reflect(s) current market assessments of:

- The time value of money; and
- The risks specific to the asset for which the future cash flow estimates have not been adjusted.

Cash-generating units and goodwill

For the purpose of impairment testing, goodwill acquired in a business acquisition will be allocated from the acquisition date for each cash-generating units or groups of cash-generating units of the acquirer, which are expected to benefit from the synergies of the acquisition, irrespective of whether other assets or liabilities of the acquiree are assigned to those units or groups of these units. Each unit or group of units to which goodwill has been allocated as mentioned above, will represent the lowest level of the entity in which goodwill is monitored for internal management purposes and not be larger than an operating segment as defined in the standard, IFRS 8 before the aggregation of similar segments.

Examination of Goodwill Impairment

Examination of goodwill impairment will be performed by comparing the book value of the unit, including goodwill, to its recoverable amount. If the recoverable amount of the unit exceeds the book value of the unit, goodwill allocated to the unit will be considered as not impaired. If the book value of the unit exceeds the recoverable amount of the unit, the entity shall recognize an impairment loss.

Methodology

Recognizing and measuring an impairment loss

If, and only if, the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset shall be reduced to its recoverable amount. That reduction is an impairment loss.

An impairment loss shall be recognized immediately in profit or loss, unless the asset is carried at revalued amount in accordance with another Standard.

The impairment loss shall be allocated to reduce the carrying amount of the assets of the unit (group of units) in the following order:

- (a) First, to reduce the carrying amount of any goodwill allocated to the cash-generating unit (group of units); and
- (b) Then, to the other assets of the unit (group of units) pro rata on the basis of the carrying amount of each asset in the unit (group of units).

In allocating an impairment loss, an entity shall not reduce the carrying amount of an asset below the highest of:

- (a) Its fair value less costs of disposal (if determinable);
- (b) Its value in use (if determinable); and
- (c) Zero.

Section 4

Examination of Goodwill Impairment

Examination of Goodwill Impairment

General

Determining an Impairment Loss

Frutarom's management requested that the examination of goodwill impairment will be carried out according to international accounting standards of IAS 36.

In accordance with IAS 36 annual examination of goodwill impairment of a cash-generating unit may be performed at any time during an annual period, provided the test is performed on the same date each year. Frutarom's management has determined the date of assessment of impairment of goodwill will be December 31 annually.

Identifying the cash-generating unit

In accordance with IAS 36, goodwill deriving from a business acquisition will be allocated to the cash-generating unit, which is expected to benefit from the synergies of the acquisition. The standard defines a cash-generating unit as the group of the smallest identifiable asset, generating cash inflows that are largely independent of the cash inflows from other assets. For additional details, see the methodology section below.

Frutarom's management determined that Savory activities, is the smallest cash-generating unit which the goodwill arising from the acquisition can be assigned to..

General

The recoverable amount of the cash-generating unit

In accordance with IAS 36 the recoverable amount of the larger between cash-generating unit is fair value less costs of sales and its usage value, additional details, see the methodology section below.

To assess the value in use of the cash-generating unit, we estimate that the income approach, the discounted cash flow method (Discounted Cash Flows), is the most appropriate for the valuation. For more details on valuation approaches and methodologies, see Chapter valuation approaches.

The pro forma balance sheet shows that the carrying amount of flavor operations in the US, as of December 31, 2014 is approximately $113,454 thousand.

Cash-generating unit book value

In accordance with IAS 36, the book value of the cash generating unit shall be consistent with the recoverable amount. The book value includes the book value of assets and liabilities that can be directly attributable to the cash-generating unit, which generates the future cash inflows that determines the value using the discount cash flow method.

In order to determine the book value of the cash generating unit we received from management the book value of Frutarom as of December 31, 2014. Due to the fact that the book value includes only operational assets and liabilities (excluding net financial liabilities and assets surplus), the recoverable amount of the cash generating unit was examined accordingly.

Impairment Examination of Goodwill

General

An analysis of the activity of the pro forma balance sheet shows that the book value of activity, as of December 31, 2014 is approximately 125,234 thousand Euros.

Impairment Examination of Goodwill

In accordance with IAS 36, impairment examination of goodwill will be performed by comparing the book value of the unit including goodwill to its recoverable amount. If the recoverable amount of the unit exceeds the book value of the unit, the unit and the goodwill allocated to the unit will be considered as not impaired. If book value of the unit exceeds the recoverable amount of the unit, the entity shall recognize an impairment loss.

Estimation of the recoverable amount

Measurement of the recoverable amount is determined by the value of operations. Valuation of operations will be based on the implementation of the three approaches, as described below. The approaches take into account the type of assets, the condition of the firm, and the information available to the analyst.

Income Approach

The income approach is based on the premise that the value of a security or asset is the present value of the future earning capacity that is available for distribution to investors in the security or asset. A commonly used methodology under the income approach is a discounted cash flow analysis. A discounted cash flow analysis involves forecasting the appropriate cash flow stream over an appropriate period and then discounting it back to a present value at an appropriate discount rate. This discount rate should consider the time value of money, inflation, and the risk inherent in ownership of the asset or security interest being valued.

Market Approach

The market approach references actual transactions in the equity of the enterprise being valued or transactions in similar enterprises that are traded in the public markets. Third-party transactions in the equity of an enterprise generally represent the best estimate of fair market value if they are done at arm's length. In using transactions from similar enterprises, there are two primary methods. The first, often referred to as the Guideline Transactions Method, involves determining valuation multiples from sales of enterprises with similar financial and operating characteristics and applying those multiples to the subject enterprise. The second, often referred to as the Guideline Public Company Method, involves identifying and selecting publicly traded enterprises with financial and operating characteristics similar to the enterprise being valued. Once publicly traded enterprises are identified, valuation multiples can be derived, adjusted for comparability, and then applied to the subject enterprise to estimate the value of its equity or invested capital.

Cost Approach

This method that surmises that the price someone should pay for an asset should not exceed what someone would have to pay to replace with an equivalent. In cost approach pricing, the market price for the asset is equivalent to the replacement value of the asset less depreciation. The use of this approach will be made especially in cases where there is no reliable information available and similar firms and / or was not

Impairment Examination of Goodwill

General

Possible to rely on future cash flow projections.

For this examination we will use the income approach using discounted cash flow method. According to this approach, we will build the future cash flows; the Company is expected to make a reasonable scenario, based on the parameters, which are described below. Later, future cash flows are discounted at a pre-tax discount rate, which is suitable for the type of activity reflecting the proper risk level.

Revenues

The following table presents the Company's US operations estimated revenues according to our forecast and the actual revenue results, for the years 2013-2014 (thousands of USD):

$000	2013	2014	2015	2016	2017	2018	2019	Terminal
Revenue	65,850	70,272	73,786	77,475	80,574	82,991	85,066	87,192
Growth rate		*6.7%*	*5%*	*5%*	*4%*	*3%*	*2.5%*	*2.5%*

Source: BDO analysis and Management's projections

As stated on December 11, 2013, Frutarom signed an agreement to acquire 100% of Hagelin Holdings US in exchange for $52.4 million. The acquisition was completed on the signature date. Hagelin's sales turnover for the year ended December 31, 2013 was $ 23.6 million.

Sales from US and Canada customers are the main source of income. In addition, there are revenues from customers in El Salvador, Mexico, Japan and Costa Rica, and other countries, on a smaller scale.

In 2013 operating income amounted to about $65,850 thousand and also includes the Hagelin operations. In 2014 operating income amounted to about $70,272 thousand. Operating income increased by 6.7% between 2013 and 2014.

In order to determine the growth rate of activity in 2015, we examined the Company forecasts conservatively. Company forecast a growth rate of 5% depending on the type of activity and the expected growth rate of the industry.

Impairment Examination of Goodwill

Revenue projections

The Company intends to continue to coordinate sales and marketing efforts, in order to achieve our growth. Projected growth rates are based on the organic growth of the entire business, particularly in light of mergers and acquisitions completed in 2013, and future mergers and acquisitions help continued growth through exposure to markets and new customers.

The rest of the years of the forecast, it was assumed that operating income growth will gradually decrease from 5% in 2015 to a rate of 2.5% per year, which represents, in accordance with the terminal growth of the Company.

Cost of Sales

The following table presents the forecasted cost of sales according to our estimations, and the actual cost of sales results, for the years 2013-2014 (thousands of USD)

$000	2013	2014	2015	2016	2017	2018	2019	Terminal
Cost of sales	33,471	37,048	38,715	40,461	41,923	43,062	44,037	45,036
% of revenue	*50.8%*	*52.7%*	*52.5%*	*52.2%*	*52.0%*	*51.9%*	*51.8%*	*51.7%*

Source: Source: BDO analysis and Management's projections

Cost of sales includes: costs of raw materials; Salaries and related expenses; Rental expenses; Depreciation and amortization, energy and other expenses

In 2013, cost of sales of US operations was approximately $33,471 thousand, representing 50.8% of total revenues. In 2014, cost of sales was approximately $37,048 thousand, representing 52.7% of total revenues.

Therefore, we have relied on the Company's budget for 2015, according to which cost of sales margin declined in 2015 to about 52.5% of revenues. We believe that, given the efficiency measures taken by the Company, both in production processes and with suppliers, cost of sales will decrease to about 51.8% in the terminal year. For this forecast we analyzed to predict the variable and fixed variable of cost of sales, including the change in the volume of these expenses in relation to changes in the volume of revenues. In the long run it was assumed that this cost will increase in accordance with the terminal growth rate of activity.

.

Impairment Examination of Goodwill

Gross profit

The following table presents the Unit's estimated forecasted gross profit and the actual gross profit results, for the years 2013-2014 (thousands of USD)

$000	2013	2014	2015	2016	2017	2018	2019	Terminal
Gross profit	32,379	33,224	35,071	37,014	38,651	39,929	41,029	42,157
Gross margin	*49.2%*	*47.3%*	*47.5%*	*47.8%*	*48.0%*	*48.1%*	*48.2%*	*48.3%*

Source: BDO analysis and Management's projections

As a result of the assumptions described, the table shows that the gross profit margin forecast will be about 47.5% in 2015 and will rise to about 48.2% at terminal year.

Sales and Marketing

The following table presents the Unit's estimated S&M expenses according to our forecast, and the actual S&M expenses results, for the years 2013-2014 (thousands of USD):

$000	2013	2014	2015	2016	2017	2018	2019	Terminal
S&M	7,187	5,767	6,012	6,269	6,482	6,648	6,790	6,934
% of revenue	*10.9%*	*8.2%*	*8.1%*	*8.1%*	*8.0%*	*8.0%*	*8.0%*	*8.0%*

Source: BDO analysis and Management's projections

The Unit's S&M expenses consisting mainly of employee wages, advertising, commission's fee, overhead expenses and other expenses.

In 2013, selling and marketing expenses of US operations were approximately $7,187 thousand, representing 10.9% of total revenues. In 2014, these expenses weret approximately $5,767 thousand, representing a rate of 8.2% of total revenues. This decline in sales and marketing expenses is due to the termination of the Company's operations in North-Bergen and relocation to Cincinnati. Synergies occurred as a result of this transition, leading to savings in sales and marketing expenses.

In order to forecast sales and marketing expenses, we analyzed the variables and fixed variables of sales and marketing expenses, including the change in the volume of sales and marketing expenses in relation to changes in the volume of revenues. Based on the Company's budget for 2015, it was assumed that sales and marketing expenses will be approximately $6,012 thousand representing 8.1% of operating revenues. For the remainder of the forecast period, it was assumed that these expenses will gradually be reduced to about 8% as in the terminal year.

Impairment Examination of Goodwill

General and Administrative

The following table presents the Unit's estimated G&A expenses according to our forecast, and the actual G&A expenses results, for the years 2013-2014 (thousands of USD):

$000	2013	2014	2015	2016	2017	2018	2019	Terminal
G&A	5,827	4,765	4,884	5,007	5,107	5,183	5,248	5,314
% of revenue	*8.8%*	*6.8%*	*6.6%*	*6.5%*	*6.3%*	*6.2%*	*6.2%*	*6.1%*

Source: BDO analysis and Management's projections

The Unit's G&A expenses consist mainly of relevant employee rent expenses, office expenses, vehicles expenses and other expenses.

In 2013, the G&A expenses were approximately $5,287 thousands, which reflect 8.8% of revenues. In 2014, the G&A expenses were about $4,765 thousand, which reflect 6.8% of revenues.

The Company's budget for 2015 assumed that general and administrative expenses in 2015 will be approximately $4,884 thousand will represent 6.6% of revenues. In the remaining years of the forecast, it's assumed that these expenses will be reduced gradually to a rate of about 6.2% at terminal year. For this forecast, we analyzed the variables and fixed variables of general and administrative expenses, including the change in the volume of these expenses in relation to changes in the volume of revenues. In the long run it was assumed that these expenses will increase in accordance with the long-term growth rate of activity.

Research and Development

The following table presents the Unit's estimated R&D expenses according to our forecast, and the actual R&D expenses results for the years 2013-2014 (thousands of USD):

$000	2013	2014	2015	2016	2017	2018	2019	Terminal
R&D	5,896	5,632	5,829	6,032	6,200	6,330	6,441	6,553
% of revenue	*9.0%*	*8.0%*	*7.9%*	*7.8%*	*7.7%*	*7.6%*	*7.6%*	*7.5%*

Source: BDO analysis and Management's projections

R&D expenses consist mainly of relevant employee wages, laboratory expenses, material consumption and other expenses.

In 2013 R&D expenditures were approximately $5,896 thousand, representing about 9% of total operating revenues. In 2014 R & D expenditures were approximately $5,632 thousand, representing about 8% of total operating revenues.

The Company's budget for 2015 assumed that R & D expenses will be approximately $5,829 thousand, 7.9% of revenues. For the remaining years of the forecast, its assumed that these expenses will be reduced gradually to a rate of 7.6% at terminal year. For this forecast, we analyzed the variables and fixed variables of research and development, including the change in the volume of these expenses in relation to changes in the volume of revenues. In the long run it was assumed that these expenses will increase in accordance with the long-term growth rate of activity.

Impairment Examination of Goodwill

Operating Profit

The following table presents the Unit's estimated operating profit according to our forecast, and the actual operating profit, for the years 2013-2014 (thousands of USD):

$000	2013	2014	2015	2016	2017	2018	2019	Terminal
Operating profit	13,469	17,060	18,346	19,707	20,861	21,768	22,550	23,355
Operating margin	*20%*	*24%*	*25%*	*25%*	*26%*	*26%*	*27%*	*27%*

Source: BDO analysis and Management's projections

As a result of the analysis described above, the Units' operating profit for the forecast years will range from 25% in 2015, to 27% in the terminal year.

Capital Expenditure and Depreciation

The following table presents our capital expenditure expenses and depreciation forecast and the actual depreciation and capital expenditure expenses results for the years 2013-2014 (thousands of USD):

$000	2014	2015	2016	2017	2018	2019	Terminal
Depreciation	1,335	1,100	1,155	1,201	1,237	1,268	1,300
% of revenue	*1.9%*	*1.5%*	*1.5%*	*1.5%*	*1.5%*	*1.5%*	*1.5%*
Capital expenditure	(1,094)	(1,100)	(1,155)	(1,201)	(1,237)	(1,268)	(1,300)
% of revenue	*1.6%*	*1.5%*	*1.5%*	*1.5%*	*1.5%*	*1.5%*	*1.5%*

Source: BDO analysis and Management's projections

According to forecasts by Frutarom's management, Frutarom does not expect to make significant investments in fixed assets in the near future and current investments are expected to remain at the same rate. In 2014, CAPEX amounted to approximately $1,094 thousand.

Depreciation expenses in 2014 amounted to approximately $1,335 thousand. Depreciation expense forecasts assume that the depreciation expenses will grow at a moderately pace to the point of $1,268 dollars at terminal year, 1.5% of revenues activity.

CAPEX was forecasted conservatively so that level of investment will be equal to the depreciation.

Impairment Examination of Goodwill

Working Capital

The Unit's working capital forecast was calculated based on the Unit's historical data, as of the years 2012-2013, and additional information from Management.

Working capital days were estimated to be:

- **Trade receivables days** – 40 days;
- **Inventory days -** 90 days;
- **Accounts payables days –** 55 days;
- **Other payables days -** 14 days.

Income Tax

The general requirements of IAS36 require that impairment tests are carried out exclusive of tax effects. Consequently, the discount rate used to estimate the present value of the cash flows should be calculated as a pre tax discount rate. In order to estimate the pre tax discount rate, present value was first calculated based on weighted average cost of capital. Then the suitable pre tax discount rate was calculated according to the present value (see following pages).

The tax rate used is 40% which is the US statutory tax rate. Please note that the value of the activity we added the value of the tax shield, which was obtained from Frutarom's management. The value of this tax shield due to the potential tax savings arising as a result of the right to reduce their income tax when there is excess cost arising from business combinations and asset transactions consolidated to current operations. We note that these amortization expenses are not included in the calculation of the cash flow as cash flow includes the depreciation reported on activities.

Impairment Examination of Goodwill

Discount rate (WACC)

The general requirements of IAS36 require that impairment tests are carried out exclusive of tax effects. Consequently, the discount rate used to estimate the present value of the cash flows should be calculated as a pre tax discount rate. When applying the Income Approach, the cash flows expected to be generated by a business are discounted to their present value equivalent using a rate of return that reflects the relative risk of the investment, as well as the time value of money. This return, known as the weighted average cost of capital ("**WACC**") is calculated by weighting the required returns on interest-bearing debt and common equity capital in proportion to their estimated percentages in an expected industry capital structure.

The general formula for calculating the WACC is:

WACC = Kd (D%) + Ke (E%)

WACC=	Weighted average rate of return on invested capital;
Kd=	After-tax rate of return on debt capital;
D%=	Debt capital as a percentage of the sum of the debt, preferred and common equity capital ("Total Invested Capital");
Ke=	Rate of return on common equity capital; and
E%=	Common equity capital as a percentage of the Total Invested Capital.

Discount rate (WACC)

CAPM has been empirically tested and is widely accepted for the purpose of estimating a Company's required return on capital. In applying the CAPM, the rate of return on capital is estimated as the current risk-free rate of return, plus a market risk premium expected over the risk-free rate of return, multiplied by the "**beta**" for the valued Company. Beta is defined as a risk measure that reflects the sensitivity of a Company's stock (**or capital**) price to the movements of the stock market as a whole.

The CAPM rate of return on capital is calculated using the formula:

Ke = Rf + β(Rm * Rf)+ SCP+ Sp **Where**;

Ke=	Rate of return on capital (in this case, Total Invested Capital);
Rf=	Risk free rate of return; (in this case, the interest taken is US index-linked bond yield for the period of 10 years) (Source: Bloomberg)

BDO Consulting Group Ziv Haft

Impairment Examination of Goodwill

Discount rate (WACC)

β =	Coefficient of relative risk (β) - The relative risk coefficient. This factor reflects the relative risks involved in a specific investment and is based on the correlation between the return on investment with a return on the capital market as a whole. When the coefficient is greater than 1, business is highly sensitive to changes in market conditions (ie, in the case a recession the sector will be worse off than other sectors, and in the case of an economic boom the sector will be better off than other industries). When the coefficient is smaller than 1, the value of the average business is less sensitive to changes in market conditions. Beta of operations was calculated in accordance with Frutarom's. In order to calculate the ß of Savory, we relied on the comparable companies, operating in the sector of production of flavor and fragrance raw, such as: Frutarom, IFF, Givaudan, Symrise. In addition, we neutralized the financial leverage from ß of each Company and averaged the non-leveraged ßs and added the specific financial leverage of the Company. The ß is estimated to be approximately 0.76. For purposes of calculation, the Beta was calculated over a 5 year weekly period**.**
Rm–Rf=	The market risk premium is the weighted average of the risk premium of the US market and is estimated to be 5.75% (Source: Damodaran 2014 - NYU Business School).
SCP	Small cap premium- Investment in small companies carry greater risk than investing in large, established companies. Therefore investors expect a higher return when they invest in small companies. Premium=6.01%..- Ibbotson valuation edition 2013 yearbook;
Srp	Specific Premium.

Discount rate (WACC)

Weights of debt and equity, taking into account in the WACC calculation are the average outstanding debt and equity weights of comparable companies.

After-tax discount rate of the cash-generating unit is determined was based on WACC model and on the following parameters:

Parameters	Abbrevation		Source
Unit's Debt	D/(D+E)	9%	Based on comparable companies analysis
Unit's Equity	E/(D+E)	91%	Based on comparable companies analysis
EV	**V**	**100%**	**–**
Cost Of Debt	Kd	1.59%	The Company's Cost of Debt
Tax Rate	T	39.6%	The effective tax rate for long-term, US
Beta	β	0.76	Levered Beta - According to comparable companies
Risk Free Rate	Rf	0.61%	The yield on US government bonds index-linked to (Source: Bloomberg system)years 15
Market Premium	Rm-Rf	5.75%	market risk premium of US - Damodaran
SCP	SCP	6.01%	Ibbotson
Cost Of Capital	Ke	10.99%	Rf +β*(Rm-Rf)+SCP+SRP
Weighted average cost of capital	**WACC**	**10%**	D*(1-T)*Kd+E*Ke

Source: BDO analysis.

The discount rate represented above reflects an after-tax discount rate; we have adapted it to reflect a pre-tax discount rate. The after tax discount rate is 10% while we believe that the pre-tax discount rate is approximately 13.8%.

Terminal growth rate

The terminal growth rate of 2.5% was determined based upon the real economy expected growth rate in the long term.

Impairment Examination of Goodwill

The Unit's Cash Flow

Based on the assessments above, below is the cash flow projections of 2015-2019 and actual 2013-2014 (thousands of USD)

$'000s	*2013	2014	2015	2016	2017	2018	2019	Terminal
Revenue	65,850	70,272	73,786	77,475	80,574	82,991	85,066	87,192
Growth rate	*8.3%*	*6.7%*	*5.0%*	*5.0%*	*4.0%*	*3.0%*	*2.5%*	*2.5%*
Total cost of sales	33,471	37,048	38,715	40,461	41,923	43,062	44,037	45,036
% of revenue	*51%*	*53%*	*52%*	*52%*	*52%*	*52%*	*52%*	*52%*
Gross profit	**32,379**	**33,224**	**35,071**	**37,014**	**38,651**	**39,929**	**41,029**	**42,157**
Gross margin	*49%*	*47%*	*48%*	*48%*	*48%*	*48%*	*48%*	*48%*
S&M	7,187	5,767	6,012	6,269	6,482	6,648	6,790	6,934
% of revenue	*11%*	*8%*	*8%*	*8%*	*8%*	*8%*	*8%*	*8%*
R&D	5,896	5,632	5,829	6,032	6,200	6,330	6,441	6,553
% of revenue	*9%*	*8%*	*8%*	*8%*	*8%*	*8%*	*8%*	*8%*
G&A	5,827	4,765	4,884	5,007	5,107	5,183	5,248	5,314
% of revenue	*9%*	*7%*	*7%*	*6%*	*6%*	*6%*	*6%*	*6%*
רווח תפעולי לפני מס	**13,469**	**17,060**	**18,346**	**19,707**	**20,861**	**21,768**	**22,550**	**23,355**
% of revenue	*20%*	*24%*	*25%*	*25%*	*26%*	*26%*	*27%*	*27%*
Adjustments								
Depreciation			1,100	1,155	1,201	1,237	1,268	1,300
Capital expenditure			(1,100)	(1,155)	(1,201)	(1,237)	(1,268)	(1,300)
Change in working capital			(496)	(399)	(336)	(262)	(225)	(231)
Net cash flow from operating activities			**17,849**	**19,308**	**20,525**	**21,506**	**22,325**	**23,124**
DCF			**16,735**	**15,914**	**14,871**	**13,697**	**12,499**	**115,018**

Source: BDO analysis and financial statements

Impairment Examination of Goodwill

Value

Below represents the value of the Company's operations by the value in use method:

$000	
Current value 2015-2019	73,718
Current terminal value	115,018
Total value of the activity	**188,736**

Sensitivity Analysis

The following table provides a sensitivity analysis of the recoverable amount with respect to a pre-tax discount rate and the terminal growth rate (thousands of USD):

		Discount rate (before tax)				
		14.8%	14.3%	13.8%	13.3%	12.8%
Growth rate	1.5%	166,112	172,471	179,352	186,819	194,952
	2.0%	169,793	176,530	183,844	191,808	200,515
	2.5%	173,773	180,935	**188,736**	197,262	206,620
	3.0%	178,092	185,731	194,082	203,247	213,352
	3.5%	182,795	190,973	199,950	209,846	220,810

Section 5

Recoverable Amount versus Book Value Comparison

Recoverable Amount versus Carrying Amount Comparison

Book Value

After finding the recoverable amount of the activity, as mentioned before above, we compare it to the book value of operations.

If the recoverable amount of the asset is less than the carrying amount, then the entity it is required to perform an estimation of the impairment of the asset being examined and reduce it accordingly.

In favor of finding the carrying amount of activity and goodwill associated, we examined the balance sheet data as of December 31, 2014 (thousands of USD):

$000	31.12.2014
Accounts receivable	7,148
Other receivable	2,976
Related Parties	2,007
Inventory	7,326
Net Fixed Assets	13,691
Software	232
Total operational assets	**33,380**
Accounts payable	4,080
Related Parties	6,121
Accrued expenses	2,175
Pension liability	422
Deferred tax	2,927
Total operational liabilities	**15,725**
Net assets	**17,655**
Customer relationships and knowledge, net	25,565
Goodwill	70,234
Sub total	**95,799**
Total carrying amount	**113,454**

Source: Management information

Recoverable Amount versus Carrying Amount

To observe potential impairment, the assets recoverable amount was compared to the carrying amount.

Difference calculated between the new value of the activity and the fair value of identifiable assets and liabilities will be the new goodwill. The difference between the value of goodwill is the impairment loss on goodwill.

The following table summarizes the results of the impairment examination for the Unit, under IAS 36:

$000	2014
Recoverable amount	188,736
Carrying amount	113,454
Impairment amount	**–**

Source: BDO analysis.

The analysis of the table above shows that the recoverable amount of the Unit is greater than its carrying amount, as of the Valuation Date. Therefore, Frutarom's US Division goodwill is not deemed to be impaired.

SECTION B

DIRECTORS' REPORT

B

FRUTAROM INDUSTRIES LTD.
DIRECTORS' REPORT ON THE COMPANY'S STATE OF AFFAIRS
FOR THE PERIOD ENDING DECEMBER 31, 2014

BOARD OF DIRECTORS' DISCUSSIONS ON
THE COMPANY'S STATE OF BUSINESS

A. REVIEW OF ACTIVITY

Frutarom Industries Ltd. (the **"Company"**) is a global company established in Israel in 1933. Frutarom became a public company in 1996 upon registration of its shares for trade on the Tel Aviv Stock Exchange. In February 2005, the Company's Global Depository Receipts were also listed on the London Stock Exchange Official List. The Company, itself and through its subsidiaries ("**Frutarom**" or the **"Group"**) develops, produces and markets flavors and fine ingredients used in the manufacture of food, beverages, flavors, fragrances, pharmaceuticals/nutraceuticals, cosmetics and personal care products. Frutarom operates production facilities in Europe, North America, Latin America, Israel, Asia and Africa, marketing and selling over 31,000 products to more than 16,000 customers in more than 150 countries and employing some 3,100 people throughout the world.

Frutarom operates in the framework of two main activities which constitute its core activities: the Flavors activity and the Specialty Fine Ingredients activity (the "**core businesses**").

- **Flavors Activity** – Frutarom develops, produces, markets and sells sweet and savory flavor solutions, including flavor and other solutions which in addition to flavors also contain fruit or vegetable ingredients and other natural ingredients (food systems) which are used mainly in the manufacture of foods, beverages and other consumed products. Frutarom develops thousands of different flavors for its customers, most of which are tailor-made for specific customers. It also develops new products to meet changing consumer preferences and future customer needs. In accordance with the Company's strategy, Frutarom's flavor activity has grown rapidly and profitably by combining organic growth and acquisitions, and in 2014 accounted for 80% of the Company's core activity and 72% of its overall sales (as opposed to 33% of overall sales in 2000).

  This accelerated growth is the result of focusing on the fast growing area of natural flavors, on development of innovation-based unique solutions combining taste and health for the market segment made up of large multi-nationals, focusing on mid-size and local customers in emerging and developed markets – and private label manufacturers in particular, emphasizing the provision of customized services, including technological and marketing support and assistance in the development of products; the offer of high level tailor-made services and products, as are normally provided for large multinational companies and as the result of Frutarom's strategic acquisitions, which have and are being successfully incorporated with Frutarom's global activities.

- **Specialty Fine Ingredients Activity** – Frutarom develops, produces, markets and sells natural flavor extracts, natural functional food ingredients, natural pharmaceutical/nutraceutical extracts, natural algae-based biotechnical products, natural colors, natural antioxidants that help in providing solutions in the field of food protection, essential oils, unique citrus products, aroma chemicals, and natural gums and stabilizers. The Specialty Fine Ingredients products are sold primarily to the food, beverage, flavor, fragrance, pharmaceutical/nutraceutical, cosmetics and personal care industries.

  In its Specialty Fine Ingredients activity, Frutarom focuses on developing a portfolio of high value-added niche products which give Frutarom a competitive edge over its rivals. Most of the specialty fine ingredients in taste and health are natural products which enjoy higher-than-average demand compared to non-natural products. In recent years Frutarom has been putting an emphasis on the expansion of its natural product portfolio, with particular emphasis on the area of natural, functional and healthy foods. Specialty fine ingredients activity accounted for 18% of Frutarom's overall sales in 2014.

- **Trade & Marketing** – in addition to its core business, Frutarom also imports and markets various raw materials that it does not itself manufacture as part of the service offered to customers, which includes providing them with a comprehensive solution to their needs. This Trade & Marketing activity is synergetic and supports Frutarom’s core business by leveraging its global sales organization, supply chain and purchasing systems, as well as global management, and allows Frutarom to offer a wider variety of products and more solutions and added value to its customers, mainly those in the mid-sized and domestic categories in emerging markets, and strengthen its partnership with them. This activity, which greatly expanded following the acquisitions of Etol, PTI and Montana Food, focuses mainly on Central and Eastern Europe, Latin America and Israel. In 2014 sales from this activity accounted for 10% of total Frutarom activity.

RAPID GROWTH STRATEGY – PROFITABLE ORGANIC GROWTH AND STRATEGIC ACQUISITIONS

Frutarom continues to resolutely implement its rapid profitable growth strategy while strengthening its research and development, supply chain and manufacturing, and sales and marketing infrastructures along a continuing search for additional strategic acquisitions.

- **Increasing the Share of the Flavors’ Activity** – The successful implementation of Frutarom’s rapid and profitable growth strategy has allowed Frutarom to significantly increase its activities in the Flavors segment, the more profitable of its activities, achieving growth at a higher rate that the markets in which it operates. Revenues from the Flavors activity now constitute 72% of Frutarom's total revenues (compared to 33% in 2000).

- **<u>Development of New Products and Solutions Combining Taste and Health</u>** – Frutarom develops innovative taste and health solutions addressing customers' requirements and future needs. These solutions are in line with the major trends in the global food market and with consumer demand, including the combination of taste with health, health supplements, anti-aging products and food products targeting specific population and age groups. The added value offered by Frutarom and Frutarom's unique abilities to combine taste, texture, and ingredients with added health attributes give the Company an important competitive advantage among customers in both developed and emerging markets. These new and innovative products mostly have higher margins and therefore contribute not only to growth in sales but also towards improving Frutarom's product mix and profitability.

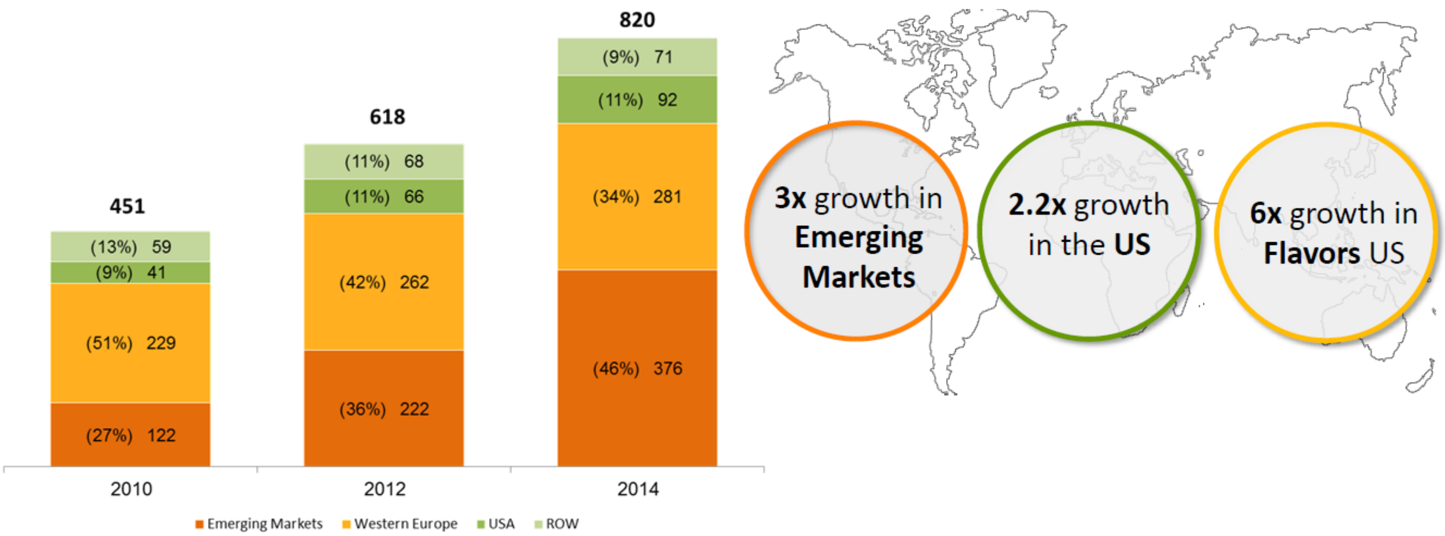
- **<u>Focus on Natural Products</u>** – Frutarom is engaged in developing and expanding its portfolio of natural products in response to consumer demand and prevalent trends in the global food industry towards healthier and more natural foods. This field is growing at a rapid pace and Frutarom's unique capabilities provide it with a competitive edge. Following this strategy, Frutarom has recently expanded its activities while also entering the field of natural food colors (through its acquisitions of Montana Food, Vitiva and Ingrenat) and significantly increasing its operations in the field of natural antioxidants for food protection solutions.

- **<u>Improvements in Specialty Fine Ingredients Product Mix</u>** – Over the past few years Frutarom has acted to improve its product mix in its Specialty Fine Ingredients activity as well. Frutarom's R&D teams have successfully developed specialty state of the art natural products, targeted for both the flavors market and the health market. The successful penetration of these products contributes to both the increase in sales of the Specialty Fine Ingredients activity and to the improvement in its margins. The latest aforementioned acquisitions will contribute towards the continuation of this positive trend.
- **<u>Strategic Change in the Geographic Mix</u>** – The successful implementation of Frutarom's strategy over the past few years, which included among other things substantial expansion of its sales in emerging markets with high growth rates and in the United States, has led to the tripling of Frutarom's revenues in 2014 in emerging markets and their doubling in the United States compared to 2010. Meanwhile the Flavors activity in the United States has grown by a factor of six.

  The rapid growth of activity outside of Western Europe has led to sales in Western Europe (which have grown by 23% since 2010) constituting 34% of Frutarom's total sales in 2014 compared with 51% in 2010. Emerging markets already account for 46% of Frutarom sales in 2014 as opposed to 27% in 2010.

  The six acquisitions carried out by Frutarom in 2013 and 2014 (JannDeRee in South Africa; PTI in Russia; Aroma in Guatemala; Hagelin in the United States, with sales also to Africa and Latin America; US-based CitraSource; and Montana Food in Peru and Chile) also contribute and will continue contributing towards Frutarom's accelerated growth and raising its market share and sales in emerging markets and the United States in which Frutarom will continue to invest and concentrate through, among other things, focused reinforcement of its R&D, production, marketing and sales platforms in important target countries and the continued execution of additional strategic acquisitions.

Frutarom continues and will continue to also expand its activity in Western European markets, leveraging its extensive product portfolio and continuing to capitalize on cross-selling opportunities.



- **Focus on Providing Quality Service and Product Development for Large Multi-national Customers and for Medium-sized Local Customers** – Frutarom continues to expand the services it provides for its customers, its product portfolio and range of solutions for both large multi-national customers and mid-size local customers, with a special emphasis on the rapidly growing private label market.

  - In the market segment of large multinational food and beverage manufacturers, Frutarom will continue to focus on products that are innovative and unique, and on expanding its portfolio of natural solutions for taste and health.

- In the market segment made up of mid-size and local customers, Frutarom offers the same high level of service, products and solutions tailored to their specific requirements as generally provided to large multi-national customers. Frutarom also offers mid-size and local customers and private labels, usually with more limited resources than large and multi-national customers, assistance in the development of their products, while providing market support and flexibility regarding minimal quantities and delivery dates.

- **Acquisitions and Mergers, and their Contribution towards Achieving Profitable Growth** – Frutarom has extensive experience with successful execution of acquisitions and mergers, and it acts to integrate the acquired companies and activities into its existing business, utilizing commercial and operational synergies to leverage the many cross-selling and operational savings opportunities and achieve continued improvement of its margins.

  After having made five strategic acquisitions in 2011 and three at the beginning of 2012, all of which were successfully integrated with its global activities and contribute to both revenues growth and improved profitability, Frutarom continued carrying out its acquisition strategy with a focus on expanding its sales and market share in emerging markets and the United States, acquiring in 2013 JannDeRee in South Africa, PTI in Russia, Aroma in Guatemala and Hagelin in the US. At the beginning of 2014 Frutarom acquired CitraSource in the US and in October 2014 the flavors and natural colors division of Montana S.A. of Peru with operations in Peru, Chile, and other countries in the region. The integration of these six acquisitions is moving forward successfully and according to plan, along with tapping to the highest degree possible the many cross-selling opportunities and operational, marketing, and technological synergies they have contributed. In addition, in February 2015 Frutarom acquired three more companies: Vitiva in Slovenia, FoodBlenders in the UK, and Ingrenat in Spain; and is working towards successfully integrating them and fully tap the strong potential they bring to the Group.

  - **Acquisition of CitraSource** – On February 24, 2014 Frutarom acquired the business activity and assets of the American company CitraSource LLC located in Florida ("**CitraSource**") for a net amount of US$7.1 million plus a performance-based future payment.

    This acquisition strengthens Frutarom’s position as a leading global manufacturer in the area of specialty citrus products. CitraSource specializes in research and development, production, marketing and sale of specialty citrus solutions to leading global customers in the flavors and aroma, food and beverages markets. CitraSource also has global purchase capabilities in the field of citrus which contribute towards strengthening Frutarom’s global purchase system. CitraSource's activities have been integrated into Frutarom's Specialty Fine Ingredients division as of March 1, 2014.

For further information on the acquisition of CitraSource, see the Company's immediate report issued on February 25, 2014.

- **<u>Acquisition of Montana Food</u>** – On October 13, 2014 Frutarom signed an agreement for the purchase of the flavors and natural colors division of Montana S.A. of Peru ("**Montana Food**") and the activity of Montana Food in Chile in exchange for a cash payment of approx. US$ 25 million and the assumption of approx. US$ 7 million in debts. The purchase agreement includes a mechanism for future consideration which depends on improvement over the current gross profit of the acquired operations.

  Montana Food is a division of longstanding Montana S.A. which was founded in 1964 and has grown into one of South America's leading companies in the field of flavors and natural food colors. Its customers include some of the world's leading global food, beverages and flavor companies as well as manufacturers based locally in South America and Central America. Sales of flavors and natural food colors, which constitute Montana Food's core activity, reached US$ 29.5 million in 2013.

  Montana Food also maintains trade and marketing activity through which, as part of its service and the providing of comprehensive solutions to its customers, it markets ingredients that it doesn't itself produce. The scope of this activity, which has been integrated into Frutarom's trade & marketing activity (which does not constitute its core activity) reached US$ 23 million in 2013

  This acquisition made Frutarom the only global player in its industry with a sizable production site in Peru as well as one of the top R&D, sales and marketing, and distribution infrastructures in the region. Frutarom will work towards capitalizing on and integrating the acquired activity's R&D and sales and marketing infrastructure in order to leverage and realize the abundance of cross-selling opportunities this acquisition presents by expanding both the customer base and the portfolio of products. The acquisition also constitutes a significant reinforcement of Frutarom's activities in the growing field of natural food colors, and it intends to leverage the capabilities of Montana Food and invest in a substantial expansion of its global activity in this important field.

  For further information on the acquisition of Montana Food, see the Company's immediate reports issued on September 30, 2014 and October 14, 2014.

- **Acquisition of Vitiva** – On February 4, 2015 Frutarom completed the purchase of 92% of the share capital of the Slovenian company Vitiva Proizvodnja in storitve d.d. ("**Vitiva**") which grants it the right to acquire 100% of Vitiva's share capital, in exchange for a cash payment of approx. US$ 10.0 million.

  Vitiva specializes in the research and development, production, marketing and sales of specialty natural extracts from plants exhibiting antioxidant activity or scientifically proven health attributes backed up by clinical studies and of natural colors for customers in the food, pharmaceutical, nutraceutical, and cosmetics markets. Among its customers are some of the world's top food, pharmaceutical, and cosmetics manufacturers. Vitiva's revenues grew from US$ 8.7 million in 2013 to US$ 11.0 million in 2014 (a 26% increase). Its activity will be integrated into Frutarom's Specialty Fine Ingredients division.

  Vitiva has many years of experience and excellent capabilities in extracting active elements from plants (particularly rosemary, olive and citrus, among others) and this will help Frutarom expand its portfolio of natural products for the food industry as well as in the fields of health and cosmetics. In addition, Vitiva has R&D abilities and a pool of knowledge based on longstanding research for continuing to expand its current product portfolio and toward entry into other fields such as the field of pet food and livestock feed preservation. Combining these abilities with Frutarom's capabilities in the field of antioxidants, particularly in the area of food protection and the lengthening of shelf life based on natural substances, will further strengthen Frutarom's position as a leading player in R&D, production, and sales for these types of solutions. The natural food colors activity joins the natural food colors activity of Montana Food and Ingrenat, advancing the implementation of Frutarom's strategy for penetrating this burgeoning field with the intention of continuing to invest in a major expansion of its global activity in this growing area.

- **Acquisition of FoodBlenders** – On February 3, 2015 Frutarom purchased 100% of the shares of UK-based FoodBlenders Limited ("**FoodBlenders**") for a cash payment of approx. US$ 2.4 million plus, conditional on performance, an additional payment expected to stand at about US$ 600,000.

  FoodBlenders, founded in 1998, engages in the development, manufacture and marketing of savory flavor solutions which mainly include spice and seasoning mixes, functional ingredients, marinades and sauces for the food industry, with particular emphasis on the convenience foods segment. In 2014 FoodBlenders posted sales of approximately US$ 3 million with profit margins similar to those of Frutarom in the same area of activity. FoodBlenders develops, manufactures and markets its products at a site in England not far from the Frutarom site at Wellingborough, and has a wide customer base which includes British food and private label manufacturers.

FoodBlenders' product line and technologies complement the product portfolios and activities of UK-based Savoury Flavours and EAFI which were acquired by Frutarom in 2012 and 2011 respectively and which also specialize in savory flavor solutions. The proximity to the Frutarom site at Wellingborough and the complementary line of products promise to generate significant synergies between FoodBlenders' activity and Frutarom's expanding savory activity in the UK and throughout the world.

- **<u>Acquisition of Ingredientes Naturales Seleccionados</u>** – On February 3, 2015 Frutarom purchased 100% of the share capital of the Spanish company Ingredientes Naturales Seleccionados ("**Ingrenat**") in exchange for approx. US$ 8 million plus an additional amount of approximately US$ 1.1 million depending on Ingrenat's performance in 2015.

  Ingrenat specializes in the research and development, production, and sales and marketing of natural extracts from plants (including, among others, paprika, rosemary, bixin, alfalfa and more) which deliver taste, color, and antioxidant activity solutions for the food industry. Numbering among its customers are food manufacturers and leading flavor, fragrance, and natural color producers. Ingrenat's sales grew 10% in 2014 to approx. US$ 9.8 million. The value of its net assets (not including cash or debt) in 2014 stood at US$ 6.9 million. Ingrenat's operations will be integrated into the activities of Frutarom's Specialty Fine Ingredients division with which they share similar profitability margins.

  The acquisition of Ingrenat is a continuation of the implementation of Frutarom's strategy of deepening and expanding its activity in the growing field of natural food colors and antioxidants, and it will continue investing towards substantially expanding its global activity in this important and growing area. The natural food colors activity joins the natural colors activity of Montana Food and Vitiva. Ingrenat's activity in antioxidants based on natural substances, particularly in the field of food protection and extension of shelf life, further reinforces Frutarom's line of solutions in this area that also gained a substantial boost with the acquisition of Vitiva which has activity in this growing field as well.

Frutarom is well positioned business-wise and competitively to continue implementing its rapid and profitable growth strategy through, among other things, carrying out further strategic acquisitions in its core business fields and main target markets. Frutarom's proven experience in successfully executing and integrating its acquisitions and tapping the their inherent cross-selling opportunities and synergies, together with a strong acquisition pipeline, will allow the Company to continue meeting its strategic goals, expand its portfolio of natural and specialty products combining taste and health solutions, and continuing to expand its activity in emerging markets and the US and to improve the operational efficiency of its resources.

- **Increase in Profit and Profit Margins** – Over recent years Frutarom has succeeded in attaining, along with its growth in revenues, significant increases in profits and in its gross and operating margins. Frutarom is working and will continue to work on strengthening its competitiveness while boosting profits and profitability by focusing, among other things, on the following objectives:

    - **Successful integration of acquisitions while maximizing synergies** – Integration of the eight acquisitions made in 2011 and 2012 has been successfully completed, and according to plan have contributed and will keep contributing to growth in sales and to improved profits and margins. Frutarom continues working towards capitalizing on the abundant cross-selling opportunities arising from these acquisitions, gaining maximum advantage from the many technological capabilities brought to the Company, and realizing the savings resulting from the integration of R&D, sales, marketing, supply chain, operations and purchasing systems. Integration of the six acquisitions made in 2013 and 2014 is moving forward successfully. These acquisitions are contributing and will keep contributing to Frutarom's continued growth in sales and profits in the coming years. The successful integration of the three acquisitions performed at the beginning of 2015 (Vitiva, Ingrenat, and FoodBlenders) is also expected to contribute towards the continuing trend of improvement in Frutarom's results.

    - Investing in R&D for **natural specialty products in the fields of taste and health** which contribute to improving the product mix and Frutarom's profitability.

    - **Integration of R&D systems** – Frutarom is working to make maximum utilization of the many innovative R&D and technological capabilities gained over recent years through its acquisitions, as well as implementing its new customer relationship management (CRM) system and cross-organizational joint R&D and applications projects for broadening its product portfolio, and improving the quality of solutions and level of service to customers, channeling the projects to the relevant know-how centers and leveraging the knowledge and expertise developed at the various Frutarom sites over recent decades.

    - **Building up and strengthening the global purchasing system** – Frutarom continues to build and strengthen its global purchasing infrastructure, leveraging its size following the recent acquisitions, while expanding its pool of suppliers with emphasis on increased purchase of raw materials (especially natural raw materials) used in the manufacture of its products from their countries of origin. Integration of the Company's R&D systems also contributes to the strengthening of the global purchasing capacities, capitalizing on the harmonization of the raw materials and suppliers for the development and manufacture of its products.

- **Streamlining programs** – Frutarom is continuing to implement additional projects for combining and consolidating production and operational sites and towards achieving utmost efficiency also in the areas of purchasing, logistics and supply chain which will contribute to strengthening its competitive position and improving its profits and margins over the coming years.

Frutarom's sturdy capital structure (total assets of US$ 940.4 million and equity of US$ 522.0 million as of December 31, 2014 constituting 55.5% of total assets), net debt (total loans minus cash) of US$ 167.5 million as of December 31, 2014, supported by the cash flow generated and together with bank backing, will allow it to continue implementing its rapid and profitable growth strategy as it has done over the past few years, including further strategic acquisitions, while strengthening its competitiveness and position as one of the leading global companies in the field of flavors and fine ingredients, and to realize its vision:

.

"To be the Preferred Partner for Tasty and Healthy Success"

B. FINANCIAL POSITION

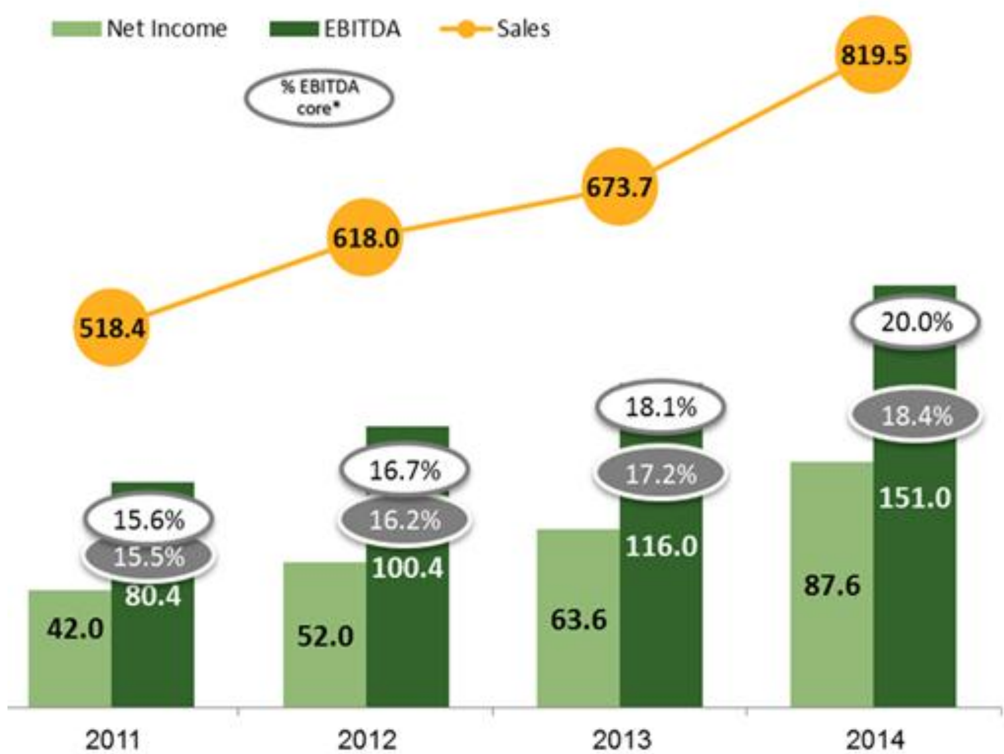
The Group's total assets as of December 31, 2014 were US$ 940.4 million compared with US$ 970.8 million as of December 31, 2013.

The Group's current assets as of December 31, 2014 totaled US$ 398.8 million compared with US$ 375.0 million as of December 31, 2013.

Property, plant and equipment net of cumulative depreciation plus other net property as of December 31, 2014 totaled US$ 538.6 million, compared with US$ 592.3 million as of December 31, 2013.

The US dollar value of total assets was affected by the significant strengthening of the US dollar against the main currencies with which the Group transacts its business (Euro, GBP, CHF and ruble), as described below, as well as by its recent acquisitions.

C. RESULTS OF OPERATIONS IN 2014



Frutarom achieved another record-setting year in 2014. Sales grew 21.6% to reach an annual record level of US$ 819.5 million. Records were also set for gross and operating profits and margins, EBITDA and EBITDA margin, as well as for net income and earnings per share.

The trend of improvement in the profit and margin of the core business, which includes the Flavors and Specialty Fine Ingredients activities, has continued. The EBITDA margin rose and reached a record 20.0% in 2014 compared with 18.1% in 2013, 16.7% in 2012 and 15.6% in 2011.

Net income grew by 37.7% in 2014, reaching US$ 87.6 million compared with US$ 63.6 million, and has more than doubled since 2011 when it stood at US$ 42.0 million.

Earnings per share rose 36.7% to US$ 1.49 compared with US$ 1.09 in 2013 and US$ 0.73 in 2011.

Sales

Frutarom sales grew by 21.6% in 2014 to reach a record high of US$ 819.5 million, compared with US$ 673.7 million in 2013.

In pro-forma terms[1] and net of currency effects, sales grew 4.9% in 2014. Exchange rate fluctuations for currencies in which the Company operates versus the US dollar reduced the annual growth in sales by 2.3% (US$ 18.8 million).

Frutarom sales in the Flavors field rose by 19.3% to reach US$ 589.8 million, compared with US$ 494.4 million in 2013, and represented 72% of total Group sales.

In pro-forma terms, sales growth for Flavors in 2014 net of currency effects reached 4.4%. Currency exchange-rate effects reduced growth by 2.1%

Frutarom sales from Specialty Fine Ingredients increased by 8.8% in 2014, reaching US$ 158.4 million compared with US$ 145.6 million in 2013.

In pro-forma terms, sales growth for Specialty Fine Ingredients in 2014 net of currency effects reached 4.4%, with currency exchange-rate effects contributing 0.3% to growth

Frutarom sales from Trade & Marketing (not a core activity of Frutarom) grew substantially following the acquisition of PTI and Montana Food, and center mainly on Central and Eastern Europe, Latin America and Israel. In 2014 sales for Frutarom in this field jumped 97.7% to reach US$ 78.5 million as opposed to US$ 39.7 million the previous year. Sales for the Trade & Marketing activity in pro-forma terms climbed 10.2% from the previous year.

[1] Assuming acquisitions performed in 2013 had been consolidated as of January 1, 2013; that CitraSource, which was acquired during the first quarter of 2014, had been consolidated as of March 1, 2013; and that Montana Food, acquired during the fourth quarter of 2014, had been consolidated as of November 1, 2013 ("**Pro-forma Terms**").

Currency Effects

The considerable strengthening of the US dollar against most other global currencies gained momentum during the final months of 2014, a trend that has also extended into the first quarter of 2015.

About 70% of Frutarom's sales are conducted in currencies other than the US dollar (mainly the Euro, Pound Sterling, Swiss Franc, Russian Ruble, New Israeli Shekel, Chinese Yuan, Brazilian Real, Peruvian Nuevo Sol and South African Rand) and changes in exchange rates affect Frutarom's reported results in US dollar terms. However, exposure to currency fluctuations is reduced by the fact that Frutarom’s raw materials purchases and operational expenditures in various countries in which it operates are also paid for in most cases in the various currencies so that most of the effect applies to the translation of sales revenues and profits into dollar terms (and not to the profitability of its various activities and/or the group's profitability).

Annual Sales Breakdown by Activity 2003-2014 (US$ millions and %)

		2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Flavor Activity	Sales	68.2	110.9	150.4	187.0	247.7	339.8	297.1	306.4	369.9	457.3	494.4	589.8
	%	49%	56%	62%	65%	67%	72%	70%	68%	71%	74%	73%	72%
Fine Ingredient Activity	Sales	67.0	81.7	89.8	98.4	115.0	124.3	123.8	141.5	145.0	140.8	145.6	158.4
	%	48%	41%	37%	34%	31%	26%	29%	31%	28%	23%	22%	19%
Inter-company Sales	Sales	-2.3	-2.6	-2.7	-4.9	-4.9	-4.0	-2.8	-2.2	-2.9	-2.4	-6.0	-7.1
Total Core Activity	Sales	132.8	190.0	237.5	280.5	357.8	460.1	418.1	445.7	512.0	595.7	634.0	741.0
	%	95%	96%	97%	98%	97%	97%	98%	99%	99%	96%	94%	90%
Trade & Marketing	Sales	6.5	6.8	6.3	6.7	10.5	13.2	7.1	5.4	6.4	22.3	39.7	78.5
	%	5%	4%	3%	2%	3%	3%	2%	1%	1%	4%	6%	10%
Total Sales		139.3	196.8	243.8	287.2	368.3	473.3	425.2	451.1	518.4	618.0	673.7	819.5

Summary of the income statements for 2013 - 2014 (US$ millions):

In 2014 Frutarom achieved record results for sales and for gross and operating profits and margins, EBITDA and EBITDA margin, net income and earnings per share.

	Core Businesses Flavors and Specialty Fine Ingredients			**Trade & Marketing**			**Total Frutarom Group**		
	2013	**2014**	**% growth**	**2013**	**2014**	**% growth**	**2013**	**2014**	***% growth***
Sales	634.0	741.0	*16.9%*	39.7	78.5	*97.7%*	673.7	819.5	*21.6%*
Gross profit	250.7	303.7	*21.1%*	6.1	16.8	*177.6%*	256.8	320.6	*24.8%*
Margin	*39.5%*	*41.0%*		*15.3%*	*21.4%*		*38.1%*	*39.1%*	
Operating profit	85.8	116.2	*35.4%*	0.9	2.7	*192.5%*	86.8	118.9	*37.1%*
Margin	*13.5%*	*15.7%*		*2.3%*	*3.4%*		*12.9%*	*14.5%*	
EBITDA	115.0	148.0	*28.7%*	1.0	3.0	*201.0%*	116.0	151.0	*30.2%*
Margin	***18.1%***	***20.0%***		***2.5%***	***3.8%***		***17.2%***	***18.4%***	
Financial expenses							7.5	10.1	*34.1%*
Income before taxes							79.2	108.8	*37.4%*
Net income							63.6	87.6	*37.7%*

Gross Profit

The gross profit for Frutarom's core businesses (which include the Flavors and Specialty Fine Ingredients activities) rose by 21.1% reaching US$ 303.7 million. The gross margin for the core businesses reached 41.0% compared with gross margin of 39.5% in 2013.

Gross profit for all Frutarom activity grew 24.8% to US$ 320.6 million (39.1% of all revenues) compared with US$ 256.8 million (38.1% of all revenues) in 2013.

Organic growth in sales, an improved product mix, and measures taken by Frutarom to increase operational efficiency have all contributed to the improvement in gross profit and margin for its core businesses in 2014. The Company continues taking action to optimize its resources also following its latest acquisitions with the creation of significant operational savings and the strengthening of its competitive position.

Frutarom is also continuing to build and strengthen its global purchasing system, utilizing its increased purchasing power from its acquisitions and is continuously expanding its pool of suppliers and with an emphasis on purchasing of raw materials used in the manufacture of its products from source countries (especially natural raw materials). The global purchasing system will also add to the trend of improvement in profit and margin.

R&D, Sales and Marketing, G&A and Other Expenses

R&D, sales and marketing, G&A and other expenses totaled US$ 201.6 million (24.6% of sales) in 2014 compared with US$ 170.0 million (25.2% of sales) the previous year.

These expenses rose largely due to the consolidation of the six activities acquired in 2013 and 2014. Frutarom, as stated, is working towards the continued successful integration of its most recent acquisitions performed in 2014 and the beginning of 2015, along with attaining maximum efficiency, improving its cost structure and strengthening its future competitive capabilities, with optimal utilization of its locations throughout the world.

R&D, sales and marketing, G&A and other expenses included nonrecurring expenses totaling US$ 1.1 million in 2014, most of which was attributable to acquisitions. In the previous year the amount of US$ 3.4 million in nonrecurring expenses was recorded, mostly attributable to acquisitions and to the closure of a Frutarom site in northern Germany and the transfer of operations there to more efficient facilities of the Company as part of its streamlining program.

Operating Profit and EBITDA

Operating profit from Frutarom’s core businesses (which include the Flavors and Specialty Fine Ingredients activities) climbed 35.4% in 2014 to reach US$ 116.2 million (15.7% of sales), compared with US$ 85.8 million (13.5% of sales) in 2013.

Operating profit from all Frutarom activities rose 37.1% in 2014 to an all-time one year high of US$ 118.9 million (14.5% of sales), compared with US$ 86.8 million (12.9% of sales) the previous year.

EBITDA from Frutarom’s core businesses (which include the Flavors and Specialty Fine Ingredients activities) rose 28.7% in 2014, reaching US$ 148.0 million (20.0% of sales) compared with US$ 115.0 million (18.1% of sales) in 2013.

EBITDA from all Frutarom activities increased by 30.2% in 2014, reaching a yearly record high of US$ 151.0 million (18.4% of sales) compared with US$ 116.0 million (17.2% of sales) the previous year.

Financial Expenses / Income

Net financial expenses for 2014 totaled US$ 10.1 million (1.2% of sales) compared with net financial expenses of US$ 7.5 million in 2013 (1.1% of sales).

Interest expense in 2014 amounted to US$ 5.9 million compared with US$ 5.6 million the previous year. A one-time financial expense of US$ 4.5 million was also recorded with respect to the revaluation of financial liabilities pertaining to purchase options on shares in PTI due to its results being stronger than anticipated.

In 2014 there was US$ 0.2 million in financial income from exchange-rate differences as opposed to US$ 1.9 million in financial expenses from exchange-rate differences in 2013.

Income before Taxes

Income before taxes climbed 37.4% in 2014 to reach a yearly record high of US$ 108.8 million (13.3% of sales), compared with US$ 79.2 million (11.8% of sales) in 2013.

Taxes on Income

Taxes on income for 2014 totaled US$ 21.2 million (19.5% of income before tax) compared with US$ 15.6 million (19.7% of income before tax) in 2013.

Net Income

Net profit for 2014 climbed 37.7% to reach a yearly record high of US$ 87.6 million, compared with US$ 63.6 million in 2013. The net margin reached 10.7% in 2014, compared with 9.4% in 2013.

Earnings per Share

Earnings per share rose 36.7% in 2014 to reach a record high of US$ 1.49 compared with US$ 1.09 the previous year.

D. RESULTS OF OPERATIONS FOR FOURTH QUARTER 2014

The fourth quarter of 2014 was yet another record setting quarter in which Frutarom attained its highest ever Q4 results in sales, which reached US$ 202.2 million, along with gross and operating profits and margins, EBITDA and EBITDA margin, as well as for net income and earnings per share.

This trend of improvement in gross and operating profits and margins is continuing. Gross margin from Frutarom's core business (Flavors and Specialty Fine Ingredients activities) climbed to 40.6% in Q4 2014, compared with 38.5% in Q4 2013. Operating margin this quarter from its core business reached 15.3%, compared with 11.6% in the same quarter last year. Core businesses EBITDA for the quarter reached US$ 35.2 million (19.5% of sales), compared with the US$ 27.8 million in the same quarter last year (16.2% of sales).

Net income grew by 31.6% in Q4 2014, reaching US$ 19.7 million compared with US$ 15.0 million in the same quarter of the previous year.

Earnings per share rose 31.1% in Q4 2014 to reach US$ 0.34 per share compared with US$ 0.26 per share in Q4 2013.

Sales

Frutarom sales in Q4 2014 grew by 5.4% to reach a fourth quarter record high of US$ 202.2 million, compared with US$ 191.8 million in Q4 2013.

In pro-forma terms and net of currency effects, organic sales growth for the quarter reached 5.5% compared with the year before. The considerable strengthening of the US dollar in relation to the other currencies in which the Company operates reduced sales in USD terms by 8.7% (in comparison with Q4 2013).

Frutarom sales in Q4 2014 from its Flavors activity increased by 6.1% to reach US$ 147.7 million, compared with US$ 139.3 during the same quarter last year, and constituted 73.1% of overall sales.

In pro-forma terms and net of currency effects, sales growth for Flavors this quarter reached 5.8% against the year before. Currency effects cut growth of Flavors activity sales by 7.9%.

Frutarom sales from Specialty Fine Ingredients amounted to US$ 34.0 million in Q4 2014 compared with US$ 33.8 million in the same quarter last year.

In pro-forma terms and net of currency effects, Q4 sales in Specialty Fine Ingredients increased by 0.5% from the year before, with currency effects reducing growth by 4.5%.

Frutarom sales from its Trade & Marketing activity (not a core activity of Frutarom) grew significantly following the acquisitions of PTI and Montana Food, and are concentrated mainly in Central and Eastern Europe, Latin America and Israel. Frutarom's Q4 2014 sales in this field climbed 10.5% to US$ 22.0 million from US$ 19.9 million in the previous year. In pro-forma terms, Frutarom's sales in the Trade & Marketing field grew year over year for the quarter by 12.2%.

Q4 Sales Breakdown by Activity 2003-2014 (US$ millions and %)

		Q4 2003	Q4 2004	Q4 2005	Q4 2006	Q4 2007	Q4 2008	Q4 2009	Q4 2010	Q4 2011	Q4 2012	Q4 2013	Q4 2014
Flavor Activity	Sales	18.5	40.1	30.8	45.5	78.5	71.3	76.6	78.1	100.1	111.7	139.3	147.7
	%	51%	70%	59%	63%	72%	72%	71%	69%	76%	77%	73%	73%
Fine Ingredient Activity	Sales	17.2	16.1	20.0	26.4	28.9	25.5	30.9	33.2	30.9	29.5	33.8	34.0
	%	47%	28%	38%	36%	27%	26%	29%	30%	23%	20%	18%	17%
Inter-company Sales	Sales	-0.6	-0.7	0.5	-1.4	-1.5	-0.8	-0.4	-0.5	-0.5	-0.7	-1.1	-1.5
Total Core Activity	Sales	**35.1**	**55.5**	**51.3**	**70.5**	**105.9**	**96.0**	**107.1**	**110.8**	**130.5**	**140.5**	**171.9**	**180.2**
	%	**96%**	**97%**	**98%**	**97%**	**98%**	**97%**	**99%**	**99%**	**99%**	**97%**	**90%**	**89%**
Trade & Marketing	Sales	1.4	1.5	1.3	2.0	2.6	2.7	1.4	1.6	1.1	4.3	19.9	22.0
	%	4%	3%	2%	3%	2%	3%	1%	1%	1%	3%	10%	11%
Total Sales		36.5	57.0	52.6	72.5	108.5	98.7	108.5	112.4	131.6	144.9	191.8	202.2

Summary of the income statements for Q4 2013 and Q4 2014 (US$ millions):

In the fourth quarter of 2014 Frutarom achieved record results in sales and gross, operating, EBITDA, and net profits and margins, along with earnings per share.

	Core Businesses Flavors and Specialty Fine Ingredients			Trade & Marketing			Total Frutarom Group		
	Q4 2013	Q4 2014	% growth	Q4 2013	Q4 2014	% growth	Q4 2013	Q4 2014	*% growth*
Sales	171.9	180.2	*4.8%*	19.9	22.0	*10.5%*	191.8	202.2	*5.4%*
Gross profit	66.1	73.2	*10.7%*	4.1	6.3	*56.3%*	70.2	79.6	*13.3%*
Margin	*38.5%*	*40.6%*		*20.4%*	*28.8%*		*36.6%*	*39.3%*	
Operating profit	19.9	27.5	*38.0%*	0.4	1.2	*198.5%*	20.3	28.7	*41.1%*
Margin	*11.6%*	*15.3%*		*2.0%*	*5.4%*		*10.6%*	*14.2%*	
EBITDA	27.8	35.2	*26.6%*	0.5	1.3	*175.9%*	28.3	36.5	*29.0%*
Margin	***16.2%***	***19.5%***		***2.3%***	***5.8%***		***14.7%***	***18.0%***	
Financial expenses							2.5	5.6	*120.8%*
Income before taxes							17.8	23.1	*29.8%*
Net income							15.0	19.7	*31.6%*

Gross Profit

Gross profit of Frutarom's core businesses (which includes the Flavors and Specialty Fine Ingredients activities) rose 10.7% in Q4 2014 to US$ 73.2 million. The gross margin from core businesses reached 40.6% compared with a 38.5% gross margin in Q4 2013.

Gross profit of overall Frutarom activity rose 13.3% to US$ 79.6 million (39.3% of overall revenues), compared with US$ 70.2 million (36.6% of overall revenues) in the same quarter of 2013.

Organic sales growth, an enhanced product mix, and actions taken by Frutarom to boost operational efficiency have all contributed to the improvement in gross profit and margin.

R&D, Sales and Marketing, G&A and Other Expenses

R&D, sales and marketing, G&A and other expenses amounted to US$ 50.8 million (25.1% of sales) in Q4 2014 compared with US$ 49.9 million (26.0% of sales) the previous year.

The increase in expenses derives from the increase in the scope of activities, mainly from the acquisitions carried out in 2013 and 2014. Frutarom has and continues to act, as stated, towards achieving maximum efficiency, improving its cost structure, developing a global purchasing system, and strengthening its future competitive capabilities, while taking full advantage of its worldwide spread of locations and successfully integrating its latest acquisitions.

In Q4 2014 the R&D, sales and marketing, G&A and other expenses included nonrecurring expenses totaling US$ 0.6 million relating mainly to acquisitions, as against US$ 1.2 million in nonrecurring expenses in Q4 2013.

Operating Profit and EBITDA

Operating profit from core businesses (which includes the Flavors and Specialty Fine Ingredients activities) rose 38.0% in Q4 2014 to US$ 27.5 million (15.3% of sales) compared with US$ 19.9 million (11.6% of sales) in the same quarter of the previous year.

Operating profit from Frutarom's overall activity in Q4 2013 climbed 41.1% to a fourth quarter record high of US$ 28.7 million (14.2% of sales) compared with US$ 20.3 million (10.6% of sales) in the same quarter of the previous year.

EBITDA for Frutarom’s core businesses (which include the Flavors and Specialty Fine Ingredients activities) rose in Q4 2014 by 26.6% to US$ 35.2 million (19.5% of sales) from US$ 27.8 million (16.2% of sales) in Q4 2013.

EBITDA from Frutarom's overall activity in Q4 2013 rose 29.0% to reach a fourth quarter record high of US$ 36.5 million (18.0% of sales), compared with US$ 28.3 million (14.7% of sales) in the comparable period.

Financial Expenses / Income

Net financial expenses in Q4 2014 amounted to US$ 5.6 million (2.8% of sales) compared with net financial expenses of US$ 2.5 million (1.3% of sales) in Q4 2013.

Interest expense in Q4 2014 amounted to US$ 1.4 million compared with US$ 2.0 million the previous year.

Also recorded in financial expenses was a one-time expense of US$ 4.5 million for revaluation of financial liabilities pertaining to purchase options on shares in PTI due to its results being stronger than anticipated.

Income before Tax

Income before taxes climbed 29.8% in Q4 2014 to reach a fourth quarter record high of US$ 23.1 million (11.4% of sales), compared with US$ 17.8 million (9.3% of sales) in Q4 2013.

Taxes on Income

Taxes on income for Q4 2014 totaled US$ 3.5 million (15.0% of income before tax) compared with US$ 2.9 million (16.1% of income before tax) in Q4 2013.

Net Income

Net income climbed 31.6% in Q4 2014 to reach a fourth quarter record of US$ 19.7 million, 9.7% of sales, compared with US$ 15.0 million in the fourth quarter of 2013 (7.8% of sales).

Earnings per Share

Earnings per share for Q4 2014 rose by 31.1%, achieving a record fourth quarter high of US$ 0.34 per share, compared with US$ 0.26 per share in Q4 2013.

Summary of the quarterly profit and loss reports for 2012 - 2014 (US$ millions):

	Q1 2012	**Q2 2012**	**Q3 2012**	**Q4 2012**	**Q1 2013**	**Q2 2013**	**Q3 2013**	**Q4 2013**	**Q1 2014**	**Q2 2014**	**Q3 2014**	**Q4 2014**
Sales Revenues	151.2	164.8	157.1	144.9	152.2	168.6	161.0	191.8	188.5	218.1	210.8	202.2
Gross Profit	54.9	61.8	58.1	51.5	57.2	66.9	62.6	70.2	73.5	85.9	81.6	79.6
Selling, Marketing, R&D, G&A and Other Expenses	37.1	40.0	38.5	37.8	38.3	41.9	40.0	49.9	49.6	50.6	50.6	50.8
Operating Profit	17.8	21.8	19.5	13.7	18.9	24.9	22.6	20.3	23.9	35.3	30.9	28.7
EBITDA	25.0	28.5	26.3	20.7	25.8	32.5	29.4	28.3	32.1	43.4	39.0	36.5
Financial Expenses	0.9	4.3	0.6	1.4	1.4	2.3	1.3	2.5	1.5	2.3	0.8	5.6
Income before Tax	16.9	17.5	18.9	12.3	17.5	22.6	21.3	17.8	22.5	33.1	30.2	23.1
Net Income	**13.5**	**13.5**	**14.4**	**10.5**	**14.0**	**17.6**	**17.0**	**15.0**	**18.3**	**25.5**	**24.2**	**19.7**

Seasonality

In recent years Frutarom's activity has been subject to seasonal fluctuations which, until the acquisition of PTI, were reflected in lower sales and profitability in the first and fourth quarters of the year (with the fourth quarter typically the weakest) and stronger results in the second quarter. Following the acquisition of PTI, where the seasonality of sales in recent years is expressed by the fourth quarter being the strongest and the first quarter the weakest in terms of sales volumes, profits, and margins, Frutarom's seasonal outlook shifted somewhat.

E. LIQUIDITY

Frutarom continues to generate strong cash flows from operating activities, which helps it cut down on its level of debt and continue carrying out strategic acquisitions while maintaining a reasonable debt level. During the fourth quarter of 2014 the Company achieved cash flow from operating activities amounting to US$ 30.3 million, similar to the US$ 30.6 million reached in Q4 2013.

Total cash flow from operating activities for 2014 reached US$ 80.8 million compared with US$ 88.7 million in 2013.

The cash flow is affected by the rapid growth, which has brought about consumption of working capital, and by an increase in tax payments attributable, among other things, to proceeds from tax refunds relating to previous years having been received in 2013 (US$ 2.7 million).

Frutarom works towards maintaining an optimal level of working capital appropriate for its rate of expected growth and will continue to do so, taking into account seasonality along with the available supply of the various raw materials it uses and their current and expected future prices.

F. SOURCES OF FINANCING

Sources of Capital

Frutarom's capital equity as of December 31, 2014 totaled US$ 522.0 million (55.5% of the balance sheet) compared with US$ 521.1 million as of December 31, 2013 (53.7% of the balance sheet).

The value of total assets was affected by the strengthening of the US dollar against the main currencies with which the Group transacts its business (Euro, Pound Sterling, Swiss Franc, Russian Ruble, New Israeli Shekel, Chinese Yuan, Brazilian Real, Peruvian Nuevo Sol and South African Rand).

Long-Term Loans Including Current Maturities of Long-Term Loans (Average)

Average long-term credit from banks in 2014 totaled US$ 200.6 million, compared with US$ 133.0 million in 2013.

Average long-term credit from banks in Q4 2014 totaled US$ 192.3 million, compared with US$ 120.6 million in 2013. The increase in credit derives from loans taken during the period to finance acquisitions.

Short-Term Credit Excluding Current Maturities of Long-Term Loans (Average)

Average short-term credit made available in 2014 to the Company from banks came to US$ 39.2 million, compared with US$ 51.8 million in 2013.

Average short-term credit made available in Q4 2014 to the Company from banks came to US$ 42.0 million, compared with US$ 84.9 million during the corresponding quarter of 2013.

Frutarom's cash balances on December 31, 2014 totaled US$ 63.9 million compared with US$ 57.6 million on December 31, 2013.

The strong cash flow from operating activities has helped reduce net debt from US$ 190.1 million on December 31, 2013 to US$ 167.5 million on December 31, 2014 even after providing the means for financing the acquisitions carried out during 2014.

Accounts Payable and Accounts Receivable (Average)

In 2014 the Company made use of US$ 108.8 million in credit from suppliers and other trade creditors, compared with US$ 88.8 million the previous year, extending US$ 146.0 million in credit to its customers as compared with US$ 125.4 million the year before.

In Q4 2014 the Company made use of US$ 104.6 million in credit from suppliers and other trade creditors compared with US$ 101.8 million in the parallel period, and extended US$ 138.1 million in credit to its customers compared with US$ 139.4 million the year before. The increase in suppliers' and customers' trade credit is largely due to the addition of accounts payable and receivable balances of recently acquired companies.

In accordance with the information presented in this report with respect to the Company's financial position, liquidity, positive cash flow it generates from operating activities, and sources of financing, and provided that there will not be any significant deterioration in its sales and/or profitability, the Company believes the cash flow it generates from current operations can be expected to cover the full repayment of its anticipated liabilities without any need for external sources of funds.

EXPOSURE TO AND MANAGEMENT OF MARKET RISKS

The Group's activity is highly decentralized. Within its core business (Flavors and Specialty Fine Ingredients) the Group produces thousands of products for thousands of customers throughout the world, using thousands of different raw materials purchased from a wide range of suppliers worldwide. The Group is not significantly reliant on any specific customer, product or supplier.

A. RESPONSIBILITY FOR MARKET RISK MANAGEMENT

Mr. Alon Granot, Executive Vice President & CFO, is the person responsible for managing market risk. Company management and its Board of Directors are kept up-to-date about material changes in the Group's level of exposure to the various risks and conduct discussions on this subject whenever necessary.

For details about Mr. Alon Granot, see Regulation 26a in Chapter D (Additional Information on the Corporation) of this set of reports.

B. DESCRIPTION OF MARKET RISKS

Raw Material Price Risks

Frutarom is dependent on third parties for its supply of raw materials. The Group purchases raw materials from a very wide range of suppliers, with no individual supplier filling over 5% of its overall raw material needs. Although there is more than one supplier for most of the raw materials purchased by Frutarom, and most of these materials are widely available, there can be no guarantee that this will continue to be the case. Furthermore, the price, quality and availability of the principal raw materials used by Frutarom, mainly in the area of natural products, are subject to fluctuations as a result of international supply and demand. Many of the raw materials used by the Group are crop-related; therefore their price, quality and availability could be adversely affected by unfavorable weather conditions. Frutarom does not normally conduct futures transactions and is exposed to price fluctuations in the raw materials it uses as dictated by changes in global price trends. Monitoring of raw material prices is done on an ongoing basis by the Company’s Executive Vice President for Global Supply Chain and Operations.

Currency Risks

About 70% of Frutarom's sales are conducted in currencies other than the US dollar (mainly the Euro, Pound Sterling, Swiss Franc, Russian Ruble, New Israeli Shekel, Chinese Yuan, Brazilian Real, Peruvian Nuevo Sol and South African Rand) and changes in exchange rates affect Frutarom's reported results in US dollar terms. However, exposure to currency fluctuations is reduced by the fact that Frutarom’s raw materials purchases and operational expenditures in the various countries in which it operates are also paid for in most cases in the various currencies so that most of the effect applies to the translation of sales revenues and profits into dollar terms (and not to the profitability of its various activities and/or the group's profitability). Nonetheless, in cases of extreme fluctuations in exchange rates, and since a large part of the raw materials used in the manufacture of Frutarom's products are paid for in US dollars, in Euros, or other currencies, there is no certainty that the Company can completely update its selling prices denominated in local currency (which is different from the currency used in buying the raw material) and maintain its margin. Most non-US dollar monetary balances derive from the local activity of subsidiaries in countries where the functional currency is not the US dollar, and therefore the translation differences on the local currency balances of each company do not affect the Group’s financial expenses and are directly attributed to the translation differences equity fund. Monetary balances in other currencies are attributed to financial expenses. Currency exposure is reviewed as necessary, and at least once every quarter. The Company does not generally undertake external hedging action nor does it use other financial instruments for protection against currency fluctuations. For more details see Note 3(a) of the Company’s December 31, 2014 financial statements attached to this report.

Interest Rate Risk

The Group’s sources of banking finance, short- and long-term, are mainly quoted in Euros, US dollars, GBP, Swiss Francs and NIS (according to the functional currency of the borrowing company) and bear variable Libor interest rates. Its policy is not to take protective measures against possible interest rate hikes and there is therefore sensitivity to changes in interest rates. As of the balance sheet date the Group did not hold any financial derivatives. As of December 31, 2014 the Company had long-term loans net of current maturities totaling US$ 164 million along with short-term debt, including current maturities of long-term loans, of US$ 68 million. The Company has a cash balance of US$ 64 million and net debt amounting to US$ 168 million.

C. CORPORATE POLICY FOR MANAGING MARKET RISK

1. The Group's management monitors market risks in the area of raw material prices and currency and interest rates on an ongoing basis. Unusual events that could influence the Group's activity, such as a severe devaluation in the currency of a country where it operates, a sharp change in interest rates, or a change in the price trend for key raw materials, are discussed by Company management and by the Board of Directors.

2. Frutarom is working to build and strengthen its global purchasing, to strengthen relations with manufacturers of raw materials in the target countries in which these are produced, and to adjust the selling price of its products as necessary and in accordance with significant fluctuations in the pricing of raw materials. The Executive Vice President of Supply Chain and Operations is responsible for managing market risk relating to raw materials prices.

3. The Group's management strives to limit both economic and accounting currency exposure by balancing the liabilities and assets in each of the various currencies in which the Group operates. The Executive Vice President and CFO is the person responsible for managing the Group's currency exposure. The Group typically takes loans in local currency at variable Libor interest rates.

4. The level of exposure is regularly evaluated by the Group’s finance department and discussed among Group management, allowing immediate response to any unusual developments in the various markets. The exposure level is also reviewed by the Company's Board of Directors from time to time.

5. Frutarom did not use financial or other instruments during the reported period to protect itself from market risks to which it is exposed.

In 2014 there was no change in the Group’s market risk management policy.

D. SUPERVISION OF RISK MANAGEMENT POLICY AND ITS IMPLEMENTATION

The exposure to raw material prices is evaluated by the Executive Vice President of Global Supply Chain and Operations, the purchasing department and activities management on a regular basis and reported to the management as necessary. Meetings are also held by Company management on a regular basis on implementing risk management policy as it relates to raw materials prices, currency and interest rates. The Executive Vice President & CFO reports to the Board of Directors on exposure to these risks at least once a year and during periods of severe changes in the state of the global economy, exchange rates, raw material prices, and interest rates.

E. LINKAGE BASES REPORT

CURRENCY EXPOSURE PER PRIMARY LINKAGE BASES AT DECEMBER 31, 2014

	US$	NIS	GBP	Euro	CHF	Ruble	Others	Total
	In US$ 000s							
Assets								
Cash and equivalents	15,020	633	4,684	22,184	1,754	3,984	15,716	63,975
Customers	35,141	9,479	13,216	39,054	5,075	13,677	24,787	140,429
Other receivables	6,578	1,112	1,913	3,767	2,119	3,994	3,764	23,247
Inventory	49,644	-	21,885	36,464	19,854	20,029	23,224	171,100
Other non-current	-	41	-	3,042	-	-	-	3,083
Fixed assets, net	47,205	-	12,641	64,179	49,771	6,108	18,895	198,799
Intangible assets, net	125,325	-	48,445	119,285	1,867	20,291	24,597	339,810
Total assets	**278,913**	**11,265**	**102,784**	**287,975**	**80,440**	**68,083**	**110,983**	**940,443**
Liabilities								
Bank credit and loans	105,835	-	27	29,861	94,798	-	925	231,446
Suppliers	14,557	5,676	5,630	18,384	4,528	493	10,503	59,771
Other current payables	8,203	8,175	7,233	7,812	5,348	3,516	6,091	46,378
Retirement benefits	793	-	-	12,537	17,569	-	92	30,991
Deferred tax	7,088	-	4,784	6,249	2,511	2,613	297	23,542
Other non-current	6,824	-	-	-	-	18,501	971	26,296
Total liabilities	**143,300**	**13,851**	**17,674**	**74,843**	**124,754**	**25,123**	**18,879**	**418,424**
Capital equity								**522,019**
Net balance	**135,613**	**(2,586)**	**85,110**	**213,132**	**(44,314)**	**42,960**	**92,104**	**0**

F. SENSITIVITY TESTS

Sensitivity to Changes in the US Dollar – New Israeli Shekel Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	**+10%**	**+5%**	**-**	**-5%**	**-10%**
Exchange rate	**4.278**	**4.083**	**3.889**	**3.695**	**3.500**
			US$ 000s		
Cash and cash equivalents	(63)	(32)	633	32	63
Customers	(948)	(474)	9,479	474	948
Other accounts receivable	(111)	(56)	1,112	56	111
Other long-term receivables	(4)	(2)	41	2	4
	(1,126)	**(564)**	**11,265**	**564**	**1,126**
Suppliers and service providers	568	284	5,676	(284)	(568)
Other payables	818	409	8,175	(409)	(818)
	1,386	**693**	**13,851**	**(693)**	**(1,386)**
Total exposure, net	**260**	**129**	**(2,586)**	**(129)**	**(260)**

Sensitivity to Changes in the US Dollar - Pound Sterling Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	**+10%**	**+5%**	**-**	**-5%**	**-10%**
Exchange rate	**0.706**	**0.673**	**0.641**	**0.609**	**0.577**
			US$ 000s		
Cash and cash equivalents	(468)	(234)	4,684	234	468
Customers	(1,322)	(661)	13,216	661	1,322
Other accounts receivable	(113)	(57)	1,133	57	113
	(1,903)	**(952)**	**19,033**	**952**	**1,903**
Bank credit	3	1	27	(1)	(3)
Suppliers and service providers	563	282	5,630	(282)	(563)
Other payables	723	362	7,233	(362)	(723)
	1,289	**645**	**12,890**	**(645)**	**(1,289)**
Total exposure, net	**(614)**	**(307)**	**6,143**	**307**	**614**

Sensitivity to Changes in the US Dollar – Euro Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	**+10%**	**+5%**	**-**	**-5%**	**-10%**
Exchange rate	**0.905**	**0.864**	**0.823**	**0.782**	**0.741**
			US$ 000s		
Cash and cash equivalents	(2,218)	(1,109)	22,184	1,109	2,218
Customers	(3,905)	(1,953)	39,054	1,953	3,905
Other accounts receivable	(305)	(152)	3,047	152	305
	(6,428)	**(3,214)**	**64,285**	**3,214**	**6,428**
Bank credit	2,986	1,493	29,861	(1,493)	(2,986)
Suppliers and service providers	1,838	919	18,384	(919)	(1,838)
Other payables	781	391	7,812	(391)	(781)
	5,605	**2,803**	**56,057**	**(2,803)**	**(5,605)**
Total exposure, net	**(823)**	**(411)**	**8,228**	**411**	**823**

Sensitivity to Changes in the US Dollar - Swiss Franc Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	**+10%**	**+5%**	**-**	**-5%**	**-10%**
Exchange rate	**1.089**	**1.039**	**0.990**	**0.940**	**0.891**
			US$ 000s		
Cash and cash equivalents	(175)	(88)	1,754	88	175
Customers	(508)	(254)	5,075	254	508
Other accounts receivable	(88)	(44)	884	44	88
	(771)	**(386)**	**7,713**	**386**	**771**
Bank credit	9,480	4,740	94,798	(4,740)	(9,480)
Suppliers and service providers	453	226	4,528	(226)	(453)
Other payables	535	267	5,348	(267)	(535)
Other long-term liabilities – See Note 4(c)	-	-	-	-	-
	10,468	**5,233**	**104,674**	**(5,233)**	**(10,468)**
Total exposure, net	**9,697**	**4,847**	**(96,961)**	**(4,847)**	**(9,697)**

Sensitivity to Changes in the US Dollar - Ruble

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	+10%	+5%	-	-5%	-10%
Exchange rate	65.632	62.649	59.666	56.683	53.699
	US$ 000s				
Cash and cash equivalents	(398)	(199)	3,984	199	398
Customers	(1,368)	(684)	13,677	684	1,368
Other accounts receivable	(141)	(70)	1,407	70	141
	(1,907)	**(953)**	**19,068**	**953**	**1,907**
Suppliers and service providers	49	25	493	(25)	(49)
Other payables	352	176	3,516	(176)	(352)
Other long-term liabilities	1,850	925	18,501	(925)	(1,850)
	2,251	**1,126**	**22,510**	**(1,126)**	**(2,251)**
Total exposure, net	**344**	**173**	**(3,442)**	**(173)**	**(344)**

Sensitivity to Changes in the US Dollar - Other Currencies Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	+10%	+5%	-	-5%	-10%
	US$ 000s				
Cash and cash equivalents	(1,572)	(786)	15,716	786	1,572
Customers	(2,479)	(1,239)	24,787	1,239	2,479
Other accounts receivable	(244)	(122)	2,435	122	244
	(4,295)	**(2,147)**	**42,938**	**2,147**	**4,295**
Bank credit	93	46	925	(46)	(93)
Suppliers and service providers	1,050	525	10,503	(525)	(1,050)
Other payables	609	305	6,091	(305)	(609)
Other long-term liabilities	97	49	971	(49)	(97)
	1,849	**925**	**18,490**	**(925)**	**(1,849)**
Total exposure, net	**(2,446)**	**(1,222)**	**24,448**	**1,222**	**2,446**

Sensitivity to Changes in Interest Rate on Fixed Rate Loans – Fair Value Risk

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	**+10%**	**+5%**	**-**	**-5%**	**-10%**
	US$ 000s				
Short-term loans - CNY	5	3	806	(3)	(5)
Total exposure to change at fair value	**5**	**3**	**806**	**(3)**	**(5)**

G. SUMMARY OF SENSITIVITY TEST TABLES

The functional currency of the majority of the Group's companies is the local currency of their respective country and therefore the currency translations of balance sheet balances of these companies do not affect the Company's profit and loss report and are directly attributed to the Company's equity (translation differences capital fund).

Sensitivity to Changes in the US Dollar – New Israeli Shekel Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	**+10%**	**+5%**	**-**	**-5%**	**-10%**
Exchange rate	**4.278**	**4.083**	**3.889**	**3.695**	**3.500**
	US$ 000s				
Total exposure, net	**260**	**129**	**(2,586)**	**(129)**	**(260)**

Sensitivity to Changes in the US Dollar - Pound Sterling Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	**+10%**	**+5%**	**-**	**-5%**	**-10%**
Exchange rate	**0.706**	**0.673**	**0.641**	**0.609**	**0.577**
	US$ 000s				
Total exposure, net	**(614)**	**(307)**	**6,143**	**307**	**614**

Sensitivity to Changes in the US Dollar - Euro Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	+10%	+5%	-	-5%	-10%
Exchange rate	0.905	0.864	0.823	0.782	0.741
	US$ 000s				
Total exposure, net	(823)	(411)	8,228	411	823

Sensitivity to Changes in the US Dollar - Swiss Franc Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	+10%	+5%	-	-5%	-10%
Exchange rate	1.089	1.039	0.990	0.940	0.891
	US$ 000s				
Total exposure, net	9,697	4,847	(96,961)	(4,847)	(9,697)

Sensitivity to Changes in the US Dollar - Ruble Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	+10%	+5%	-	-5%	-10%
Exchange rate	65.632	62.649	59.666	56.683	53.699
	US$ 000s				
Total exposure, net	344	173	(3,442)	(173)	(344)

Sensitivity to Changes in the US Dollar - Other Currencies Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	+10%	+5%	-	-5%	-10%
	US$ 000s				
Total exposure, net	(2,446)	(1,222)	24,448	1,222	2,446

Sensitivity to Changes in Interest Rate on Fixed-Rate Loans – Fair Value Risk

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	+10%	+5%	-	-5%	-10%
	US$ 000s				
Total exposure, net	5	3	806	(3)	(5)

FACETS OF CORPORATE GOVERNANCE

A. DIRECTORS WITH ACCOUNTING AND FINANCIAL EXPERTISE AND INDEPENDENT DIRECTORS

Directors with Accounting and Financial Expertise

The Company's Board of Directors has determined that the minimum number of directors with accounting and financial expertise will be set at two. This number takes into account the nature of the Company's activity, its size, the scope of its activity and the complexity of its activity. The Board believes that this minimum number will enable it to fulfill its responsibilities and requirements in accordance with the law and the Company's Articles of Association, especially with respect to its responsibility to evaluate the Company's financial status and to prepare and approve the financial reports.

As of the date of this report’s publication, the Board of Directors of the Company includes six directors with accounting and financial expertise: Dr. John J. Farber, Mr. Hans Abderhalden, Mr. Yacov Elinav, Mr. Isaac Angel, Mr. Gil Leidner and Ms. Dafna Sharir. For details regarding their skills, education, experience and knowhow, based on which the Company refers to them as directors with financial and accounting expertise, refer to regulation 26 in Chapter D of this set of reports (Additional Information on the Corporation).

Independent Directors

As of the date of this report, the Company has not adopted the instruction with respect to the ratio of independent directors (as the term is defined in the Companies Law – 1999) into its Articles of Association. The Company has four independent directors, including three external directors.

B. DETAILS ABOUT THE CORPORATION'S INTERNAL AUDITOR

The Company's Internal Auditor

Mr. Yoav Barak, CPA, was appointed internal auditor of the Company and began his work as internal auditor on January 17, 2005. The internal auditor complies with the provisions of section 146(b) of the Companies' Law 1999 and with the provisions of section 8 of the Internal Audit Law, 1992.

To the best of the Company's knowledge, the internal auditor does not hold securities of the Company.

To the best of the Company's knowledge, the internal auditor does not have material business relations or other material relations with the Group or with a related entity.

The internal auditor is not an employee of the Company, but provides the auditing services as an external contractor. The internal auditor does not fill other positions in the Company or provide additional external services.

Appointment Method

The appointment of the internal auditor was approved by the Company's Board of Directors on January 17, 2005, based on the Audit Committee's recommendation. The appointment was approved by the Company's Board of Directors after reviewing the internal auditor's education (as a CPA and economist), his experience in the field of internal auditing and his experience in various managerial positions. The Company's Board of Directors found the internal auditor to be suitable to serve in this position in light of Frutarom's size, scope of activity and complexity.

The Internal Auditor's Supervisor

The internal auditor reports to the Company's Audit Committee and to the Company's President & CEO.

Audit Work Plan

The audit work plan is an annual plan prepared by the internal auditor in coordination with the President of the Company and its management, and approved by the Company's Audit Committee. The preparation of the work plan is determined by the topics perceived as worthy of thorough analysis. The factors are determined according to their risk level with the goal of detecting faults, achieving efficiencies, ensuring the protection of the Group's assets and the compliance of the Group's procedures with the respective local laws. The annual audit work plan also includes a follow-up by the Company's management on the implementation of recommendations brought by the internal auditor and the Audit Committee. The internal auditor has independent discretion to deviate from the approved audit plan, subject to consultation with the Audit Committee. The internal audit is carried out in accordance with the approved annual audit plan and is updated as necessary in accordance with the findings of the audit. The internal audit is carried out through questionnaires and physical audits at the Company sites and held companies in Israel and throughout the world. Some of the audit topics are audited throughout the Group, while others are specific topics audited according to the annual work plan.

Auditing Outside of Israel or of Held Companies

The annual audit work plan refers to the activities of all the companies in the Group, both in Israel and abroad, including the Company's substantially held companies.

Scope of the Internal Auditor's Position

The scope of the internal auditor's position is adjusted to the Group's rate of expansion and growth. The internal auditor renders services to the Group at a scope of two and a half to three working days per week.

	Number of hours invested in internal auditing in the Company in 2014
Activity in Israel	525.5
Activity outside of Israel	639.8

The scope and level of complexity of the Group's activity were taken into account in determining the scope of the internal auditor's position.

The Internal Auditor's scope of services totaled 1,165 working-hours in 2014, compared to 1,194 working-hours in 2013.

Performing the Internal Audit

As reported to the Company by the internal auditor, the work of internal audit is conducted according to professional standards accepted in Israel and the world, including the professional standards of the Israel Institute of Internal Auditors, which ensure a professional, reliable and independent audit. The audit reports are based on the findings of the audit and the documented facts. The Board of Directors is of the opinion that the internal auditor meets the requirements set forth in the above-mentioned professional standards, taking into account the professionalism, qualifications, experience, familiarity with the Group and the manner in which he prepares, submits and presents the findings of his audit.

Open Access for the Internal Auditor

The internal auditor has free and independent access to the Group's information systems, including those of held companies (whether ordinary or computerized), to all databases and to all programs for automatic data processing of the Company and its related companies, including financial data. The internal auditor may enter any and all assets of the Company, including its held companies, and examine them.

The Internal Auditor's Report

The internal auditor prepares the audit reports in writing and submits them to the Audit Committee and to the members of the Company's management.

During the course of 2014 the Audit Committee held meetings to discuss the findings of the internal auditor on February 6, August 17, and December 28. The members of the Company's Audit Committee and the Company's President & CEO, Executive Vice President & CFO, Executive Vice President for Global Supply Chain and Operations, Global VP Legal Affairs and Corporate Secretary, and VP Finance along with other relevant managers in the Group received the audit reports prior to the Audit Committee meetings in which discussions were held on the internal auditor's findings. Relevant managers were present at the Audit Committee's meetings when the audit reports relating to their activity were reviewed, as decided by the Committee Chairman.

Board of Director's Assessment of the Internal Auditor's Activity

In the opinion of the Audit Committee, the scope, character and continuity of the internal auditor's activity and work plan are reasonable under the circumstances and fulfill the goals of the internal audit of the Company.

Compensation

The internal auditor's compensation in 2014 was NIS 296 thousand. No securities were granted to the internal auditor as part of his terms of engagement. The Company believes that this compensation will not affect the internal auditor's professional judgment. The internal auditor's remuneration is not in any way dependent on the results of his work.

C. DETAILS ON THE CORPORATION'S INDEPENDENT AUDITOR

The independent auditor of the Company is Kesselman & Kesselman, a member firm of PricewaterhouseCoopers. The assets of the consolidated companies which are audited by local accountants constitute 22% of the Company's total assets, and their revenue constitutes 32.4% of the total consolidated revenue of the Group.

The fees paid by the Company to its auditor are as detailed below:

1. Total fee for auditing services, for services related to the audit and for tax services in 2014 totaled US$ 1,576 thousand (compared to US$ 1,256 thousand in 2013) in Israel and in the subsidiaries abroad (23,184 hours in 2014 compared to 14,109 hours in 2013). The amount paid for tax services does not exceed 45% of the total fees detailed in this paragraph.

2. Other fees for additional services - the overall fees for services provided by the independent auditor which are not included in paragraph 1 above totaled US$ 65 thousand in 2014 (compared to US$ 143 thousand in 2013) in Israel and in subsidiaries abroad.

The Company's general meeting of shareholders approved the appointment of the independent auditor and authorized the Company's Board of Directors to determine its fees.

D. APPROVAL PROCEDURE FOR THE FINANCIAL STATEMENTS

The Company's financial statements are submitted for approval to the Board of Directors, the Company's overall supervising body, several days after the Board of Directors' committee for the review of the financial statements (the "**Balance Sheet Committee**") has discussed the financial statements and formed recommendations to the Board of Directors in accordance with the Companies Regulations (Instructions and Terms for the Approval Procedure of the Financial Reports), 2010 ("**Reports Approval Regulations**").

Members of the Company's Board of Directors

The Board of Directors of the Company has eight members, six of whom are directors having accounting and financial expertise as detailed above. For more details regarding the Company's Board of Directors, see regulation 26 to Chapter D of this set of reports (Additional Information on the Corporation).

Members of the Balance Sheet Committee

The members of the Balance Sheet Committee are Mr. Yacov Elinav, External Director and the chairman of the committee, Mr. Isaac Angel, External Director, and Mr. Gil Leidner, Director. It should be noted that the committee's membership is not identical to that of the Audit Committee which, in addition to the directors mentioned above also includes Ms. Dafna Sharir, an External Director. The Balance Sheet Committee members have financial and accounting expertise and the ability to read and comprehend financial reports, and have provided the Company with a written declaration to this effect. Mr. Yacov Elinav and Mr. Isaac Angel are independent directors by virtue of their status as External Directors. Mr. Gil Leidner is an independent director in accordance with the determination of the Company's Audit Committee from May 19, 2011 and the Board of Director's resolution dated August 17, 2011. For details regarding the skills, education, experience and knowhow of the members of the Balance Sheet Committee, based on which the Company refers to them as directors with financial and accounting expertise, refer to regulation 26 in Chapter D of this set of reports (Additional Information on the Corporation).

Procedures Undertaken by the Balance Sheet Committee for Forming its Recommendation to the Board of Directors

The Company's financial reports were discussed at the meeting of the Balance Sheet Committee held on March 12, 2015. Members of the committee were sent the 2014 financial statements two business days prior to the meeting. All three members of the Balance Sheet Committee attended the meeting, as well as the Company's independent auditors, the Company's President & CEO Mr. Ori Yehudai, the Executive Vice President & CFO Mr. Alon Granot, Vice President Finance Mr. Guy Gill, and Ms. Tali Mirsky, Global Vice President Legal Affairs and Company Secretary. Presentations were made at the meeting by the Company and by the independent auditors. The Balance Sheet Committee discussed at the meeting, inter alia, the estimates and evaluations in the financial reports, the effectiveness of the internal control on financial reporting, the completeness and fairness of the disclosure in the financial reports, the accounting policy adopted, the accounting handling of the Group’s material issues, and the valuations, including the assumptions and estimations on which the information in the financial reports is based. In the framework of the discussion, the Balance Sheet Committee formed its recommendations to the Board of Directors in accordance with the Reports Approval Regulations. The committee's recommendations were delivered to members of the Company's Board two business days before the Board‘s meeting at which the financial reports were discussed, which members of the Board consider a reasonable period of time in light of the scope and complexity of the recommendations.

Financial Statements' Procedure of Approval by the Board of Directors

The members of the Board of Directors receive a draft of the financial statements several days before the date of the Board meeting at which they are submitted for approval. The Company's independent auditors and members of the Company's senior management are also invited to attend the meeting, including the President & CEO Mr. Ori Yehudai, Executive Vice President & CFO Mr. Alon Granot, Executive Vice President and COO Global Supply Chain Mr. Amos Anatot, Vice President Finance Mr. Guy Gill, and Ms. Tali Mirsky, Global Vice President of Legal Affairs and Corporate Secretary or another of the Company’s legal counsel. The Company’s internal auditor, Mr. Yoav Barak, is also invited to the meeting. During the meeting, the Board of Directors discusses the recommendations of the Balance Sheet Committee regarding the financial statements, and the President & CEO and the Executive Vice President & CFO also present to the Board the Group's business and financial results for the relevant period in comparison to previous periods, with emphasis on noteworthy developments that transpired over the period. During the presentation of the Group’s results, members of Company management answer questions and address comments from the Directors. Following the presentation of the Company's financial results, the Company's independent auditors answer the Directors’ questions. In conclusion the Board of Directors votes on approving the financial statements. All of the members of the

Board of Directors were present at the Board meeting held on March 15, 2015 where the financial statements for 2014 were unanimously approved.

E. <u>SENIOR OFFICE HOLDERS' REMUNERATION</u>

(1) On January 14, 2014 the General Meeting approved the compensation policy for senior officeholders in the Company after the policy was approved by the Compensation Committee and the Company's Board of Directors. For details regarding the compensation policy, see the Company's immediate report on the matter dated December 29, 2013.

(2) On March 15, 2015 the Company's Board of Directors, following approval by the Compensation Committee of the Board of Directors (the "**Compensation Committee**") from March 12, 2015, approved the bonuses for senior office holders in the Company for 2014, which are in accordance with the compensation policy. The bonuses were approved after a detailed discussion held by the Compensation Committee and the Board of Directors with regard to each senior office holder (except for the President & CEO) individually.

In addition, the Board of Directors approved the purchase of Company shares for the purpose of granting such to office holders and others as part of the 2012 Plan. For further details regarding this resolution, see the Company's immediate report dated March 15, 2015.

DISCLOSURE CONCERNING THE COMPANY'S FINANCIAL REPORTING

A. DIVIDEND DISTRIBUTION IN 2014

On March 18, 2014 the Company's Board of Directors declared a dividend distribution of NIS 0.28 per share. On May 4, 2014 the dividend totaling US$ 4,712 thousand was paid out to shareholders.

B. EVENTS MENTIONED IN THE FINANCIAL STATEMENTS SUBSEQUENT TO THE DATE OF REPORT ON FINANCIAL CONDITION

On March 15, 2015, concurrently with the approval of the financial statements for December 31, 2014, the Company's Board of Directors resolved on the distribution of a dividend in the amount of NIS 0.38 per share for a total amount of NIS 22,291 thousand (approx. US$ 5,552 thousand as of the date of this report's publication).

C. CRITICAL ACCOUNTING ESTIMATIONS

Preparation of the Company's financial reports in accordance with IFRS demands the use of critical accounting estimates, requiring Company management to use its judgment in the process of implementing the Company's general accounting policies in order to prepare estimates and make assumptions that influence the amounts presented in the financial reports.

Below are the critical accounting estimations used in preparing the Company's financial reports; during their implementation, management was required to make assumptions regarding circumstances and events involving significant uncertainty. In using its discretion to determine these estimates, Company management relied on past experience, various facts and on reasonable assumptions in accordance with the appropriate circumstances for each estimate. Actual results may differ from management's estimates. Regarding the material accounting estimates used in preparing the Company's financial reports, see also Note 4 to the Company's financial statements dated December 31, 2014 attached to this report.

Taxes on Income and Deferred Taxes

The Company is assessed for tax purposes in numerous jurisdictions; accordingly, the Company's management is required to exercise discretion in order to determine the overall provision in respect of taxes on income. The Company records provisions in its books based on its estimates of whether additional taxes will be due. Where the final tax outcome of these matters as determined by tax authorities is different from the amounts that were initially recorded, such differences will be carried to income and loss in the period in which the final tax assessment is determined by the tax authorities.

The Company also records deferred tax assets and liabilities based on the differences between the book value of its assets and liabilities and the amounts taken into account for tax purposes. The Company regularly reviews its deferred tax assets for recoverability based on historical taxable income, projected future taxable income, the expected timing of the reversals of existing temporary differences and the implementation of tax planning strategies. If the Company is unable to generate sufficient future taxable income, or if there is a material change in the actual effective tax rates or time period within which the underlying temporary differences become taxable or deductible, the Company could be required to eliminate a portion of the deferred tax asset resulting in an increase in its effective tax rate and an adverse impact on operating results.

Severance Pay

The present value of the Company's liabilities with regard to severance pay is dependent on several factors that are determined on an actuarial basis, based on a number of assumptions. The assumptions used in the calculation of the net cost (income) in regards to severance pay include the long-term yield rate on the related severance pay funds and the rate of discount. Changes in those assumptions will impact the carrying amount of the assets and liabilities in respect of severance pay. The assumption regarding the expected yield on severance pay funds is determined uniformly in accordance with long-term historical yields.

The assumption regarding the required discount rate is determined by external actuaries at the end of each year. This discount rate shall be used in determining the estimated updated value of the future cash flows that will be required for covering the severance pay liabilities. In cases where the market of high quality corporate bonds is not sufficiently liquid to serve as a basis for determining the discount rate, the determination of the discount rate shall be based on the interest rates applicable to government bonds denominated in the currency in which the benefits will be paid and which have a term to maturity approximating the period of the relevant liabilities.
Other key assumptions relating to pension liabilities, such as future payroll raises, are based on existing rates of payroll inflation.

Provision for Contingent Liabilities

Provisions for contingent legal liabilities are recorded in the books at the discretion of Company management regarding the likelihood that the cash flows will be used to meet such liabilities, and on the basis of the management's estimate regarding the present value of the expected cash flows that would be required to meet the existing liabilities.

Provision for Impairment of Goodwill and Intangibles

The need for a provision for impairment of goodwill and intangibles is evaluated once a year with respect to the recoverable value of the Company's cash generating units. The recoverable amount of a cash generating unit is determined in accordance with the assumptions and calculations made by the Group's management.

D. EXCLUSION OF THE COMPANY'S SEPARATE FINANCIAL STATEMENT UNDER REGULATION 9(C) OF THE REGULATIONS

In its annual report for 2014 the Company did not include, in accordance with Provision 9C of the Regulations, a separate financial report (the **"Solo Report"**) due to the negligibility of the additional information of such report and the fact that the Solo Report would not add any material information for a reasonable investor, to that contained in the Company's consolidated statements.

The Company decided that the information is negligible due to the fact that the Company does not have any commercial activities of any kind and therefore the Company's results of operations have no effect on the Group's consolidated profit and loss reports. The Company does not employ workers and it does not have any sales or expenses to third parties.

All the Company's revenues (dividends and financial income on revaluation of capital notes with Frutarom Ltd.) derive from Frutarom Ltd.

As far as the balance sheet is concerned, apart from the settling of accounts with the Income Tax Authority, the Company does not have any balances vis-à-vis third parties. The only balances it has are for loans and balances vis-à-vis the (wholly-owned) companies in the Group, and land property in the amount of US$139 thousand.

The Company's management determined that as long as income from externals or from companies not wholly owned by the Company is lower than 5% of the total revenues in the consolidated financial statements, and as long as the expenses to externals or from companies not wholly owned by the Company are lower than 5% of the total expenses in the consolidated financial statements, the Company's separate financial information as set forth in Provision 9C of the Regulations is negligible and its absence will not affect the prospects of investors in the Company's shares to estimate the Company's liquidity prospects, and will not add any material information for a reasonable investor.

Company management has also examined the warning signs contained in Provision 10(14) of the Regulations and found that they do not exist.

The Board of Directors of the Company held five meetings during 2014.

The Board of Directors thanks Frutarom's management and employees for the Company's fine achievements.

Dr. John J. Farber Chairman of the Board	Ori Yehudai President & CEO

March 15, 2015

SECTION C

FINANCIAL REPORTS

FRUTAROM INDUSTRIES LTD.

2014 FINANCIAL STATEMENTS

FRUTAROM INDUSTRIES LTD.

2014 FINANCIAL STATEMENTS

TABLE OF CONTENTS

REPORT OF THE AUDITORS

To the shareholders of

FRUTAROM INDUSTRIES LTD.

Regarding the audit of the components of internal control over financial reporting in accordance with section 9B(c) to the Israeli Securities Regulations (Periodic and Immediate Reports), 1970

We have audited components of internal control over financial reporting of Frutarom Industries Ltd. and its subsidiaries (hereinafter - the Company), as of December 31, 2014. These components of internal control were set as explained in the next paragraph. The Company's Board of Directors and Management are responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of components of internal control over financial reporting included in the accompanying periodic report for the above date. Our responsibility is to express an opinion on the components of internal control over financial reporting based on our audit**.**

Components of internal control over financial reporting were audited by us according to Audit Standard no. 104 of the Institute of Certified Public Accountants in Israel "Audit of the Internal Control Components over Financial Reporting" (hereafter - "Audit Standard 104"). These components are: (1) entity level controls, including controls on the preparation process and closing of the financial reporting and general controls of information systems, (2) controls over the process of purchasing process, consumption of materials and inventory (3) controls over the sales and receivables (all of these together are called the "audited control components").

We conducted our audits in accordance with Audit Standard 104. This standard requires that we plan and perform the audit to identify the audited control components and to obtain reasonable assurance whether these control components have been maintained effectively in all material respects. The audit includes obtaining an understanding of internal control over financial reporting, identifying the audited control components, assessing the risk that a material weakness exists in the audited control components, as well as review and assessment of effective planning and maintaining of these audited control components based on the estimated risk. Our audit, for those audited control components, also included performing such other procedures as we considered necessary under the circumstances. Our audit referred only to the audited control components, unlike internal control of all material processes over financial reporting, and therefore our opinion refers only to the audited control components. In addition, our audit did not take into account the mutual influences between the audited control components and those which are not audited, and therefore our opinion does not take into account such possible effects. We believe that our audit provides a reasonable basis for our opinion in the context described above.

Kesselman & Kesselman, Building 25, MATAM, P.O BOX 15084 Haifa, 3190500, Israel
Telephone: +972 -4- 8605000, Fax:+972 -4- 8605001, www.pwc.com/il

REPORT OF THE AUDITORS (continued)

Due to inherent limitations, internal control over financial reporting in general and components of internal controls in particular, may not prevent or detect a misstatement. Also, making projections on the basis of any evaluation of effectiveness is subject to the risk that controls may become inadequate because of changes in circumstances, or that the degree of compliance with the policies or procedures may be adversely affected.

In our opinion, the company effectively maintained, in all material respects, the audited control components as of December 31, 2014.

We also audited, the Company's financial statements as of December 31, 2014 and 2013 and for each of the three years in the period ended December 31, 2014, in accordance with generally accepted auditing standards, and our report, of March 15, 2015 included an unqualified opinion on these financial statements.

Haifa, Israel
15, March, 2015

Kesselman & Kesselman
Certified Public Accountants (lsr.)
A member firm of International PricewaterhouseCoopers Limited

Kesselman & Kesselman, Building 25, MATAM, P.O BOX 15084 Haifa, 3190500, Israel
Telephone: +972 -4- 8605000, Fax:+972 -4- 8605001, www.pwc.com/il

REPORT OF THE AUDITORS

To the shareholders of

FRUTAROM INDUSTRIES LTD.

We have audited the consolidated statements of financial position of Frutarom Industries Ltd. (hereafter - the Company) as of December 31, 2014 and 2013 and the related consolidated statements of income, statements of comprehensive income, changes in equity and cash flows for each of the three years in the period ended on December 31, 2014. These financial statements are the responsibility of the Company's Board of Directors and management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of certain consolidated companies, whose assets included in consolidation constitute approximately 22% and 26% of total consolidated assets as of December 31, 2014 and 2013, and whose revenues included in consolidation constitute approximately 32.4 %, 31%, and 26% of total consolidated revenues for each of the three years in the period ended December 31, 2014. The financial information of the above consolidated companies was audited by other auditors, whose reports have been furnished to us, and our opinion, insofar as it relates to financial information included for these companies, is based on reports of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in Israel, including those prescribed by the Israeli Auditors (Mode of Performance) Regulations, 1973. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Company's Board of Directors and management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of the other auditors, the accompanying financial statements referred to above present fairly, in all material respects, the consolidated financial position of the company and its subsidiaries as of December 31, 2014 and 2013 and the consolidated results of their operations, changes in equity and their cash flows for each of the three years in the period ended on December 31, 2014, in accordance with International Financial Reporting Standards (hereafter – IFRS) .

We have also audited in accordance with standard No. 104 of the Institute of Certified Public Accountants in Israel “Audit of the Internal Control Components over Financial Reporting“, internal control components over financial reporting of the company as at December 31, 2014, and our report in March 15, 2015 included an unqualified opinion on the effectiveness of those components.

Haifa, Israel
15, March, 2015

Kesselman & Kesselman
Certified Public Accountants (Isr.)
A member firm of International PricewaterhouseCoopers Limited

FRUTAROM INDUSTRIES LTD.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

	Note	As of 31 December 2014	2013
		U.S. dollars in thousands	
Assets			
CURRENT ASSETS:			
Cash and cash equivalents	18	63,975	57,612
Accounts receivable:	15		
Trade		140,429	138,373
Other		14,551	12,442
Prepaid expenses and advances to suppliers		8,696	11,803
Inventories	16	171,100	154,721
		398,751	374,951
NON-CURRENT ASSETS :			
Property, plant and equipment – net	7	198,799	208,567
Intangible assets – net	2f,8	339,810	383,729
Deferred income tax assets	13d	3,042	3,424
Other	17	41	115
		541,692	595,835
Total assets		940,443	970,786

Dr. John Farber
Chairman of the Board

Ori Yehudai
President and CEO

Alon Granot
Executive Vice President and CFO

Date of approval of the financial statements by the Board of Directors: March 15, 2015.

	Note	2014	2013
		As of 31 December	
		U.S. dollars in thousands	
Liabilities and Shareholders' Equity			
CURRENT LIABILITIES:			
Short-term bank credit and loans and current maturities of long-term loans	9	67,750	108,226
Accounts payable:	19		
Trade		59,771	58,407
Other		46,378	52,763
		173,899	219,396
NON-CURRENT LIABILITIES:			
Long-term loans net of current maturities	9	163,696	140,113
Retirement benefit obligations, net	10	30,991	23,126
Deferred income tax liabilities	13d	23,542	34,084
Liability for put option for the shareholders of a subsidiary	5e	19,967	27,522
Other	5	6,329	5,486
		244,525	230,331
COMMITMENTS AND CONTINGENT LIABILITIES	11		
Total liabilities		418,424	449,727
EQUITY:	12		
EQUITY ATTRIBUTED TO OWNERS OF THE PARENT COMPANY:			
Ordinary shares		16,822	16,781
Other capital surplus		106,664	104,293
Translation differences	2c	(48,159)	27,296
Retained earnings		445,653	371,867
Less - cost of Company shares held by the company		(2,587)	(1,981)
Non-controlling interest		3,626	2,803
Total equity		522,019	521,059
Total equity and liabilities		940,443	970,786

The accompanying notes are an integral part of these financial statements.

FRUTAROM INDUSTRIES LTD.

CONSOLIDATED INCOME STATEMENTS

	Note	2014	2013	2012
		Year ended 31 December		
		U.S. dollars in thousands, (except for per share data)		
SALES		819,547	673,693	618,001
COST OF SALES	20a	498,995	416,897	391,742
GROSS PROFIT		320,552	256,796	226,259
Selling, marketing, research and development expenses - net	20b	140,296	115,223	104,932
General and administrative expenses	20c	60,516	52,131	49,197
Other expenses (income) - net	20d	816	2,685	(718)
INCOME FROM OPERATIONS		118,924	86,757	72,848
FINANCIAL EXPENSES– net	20e	10,089	7,528	7,240
INCOME BEFORE TAXES ON INCOME		108,835	79,229	65,608
INCOME TAX	13e	21,219	15,608	13,628
NET INCOME FOR THE YEAR		87,616	63,621	51,980
PROFIT ATTRIBUTED TO:				
Owners of the parent company	5j	86,654	63,129	51,570
Non-controlling interest		962	492	410
		87,616	63,621	51,980
		U.S dollars		
EARNINGS PER SHARE:	2v			
Basic		1.49	1.09	0.90
Fully diluted		1.47	1.08	0.90

The accompanying notes are an integral part of these financial statements.

FRUTAROM INDUSTRIES LTD.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Year ended 31 December		
	2014	**2013**	**2012**
	U.S. dollars in thousands		
Income for the year	87,616	63,621	51,980
Other comprehensive income:			
Items that will not be reclassified subsequently to profit or loss:			
Remeasurement of net defined benefit Liability, net after tax	(8,156)	2,153	(4,756)
Items that could be reclassified subsequently to profit or loss:			
Translation differences	(75,504)	10,622	4,393
Total comprehensive income for the Year	3,956	76,396	51,617
Attributable to:			
Owners of the parent company	3,043	75,829	51,207
Non-controlling interest	913	567	410
Total	3,956	76,396	51,617

The accompanying notes are an integral part of these financial statements.

FRUTAROM INDUSTRIES LTD.

CONSODLIATED STATEMENTS OF CHANGES IN EQUITY

	Note	Ordinary shares	Other capital surplus	Translation differences	Retained earnings	Cost of company shares held by the company	Total attributed to owners of parent company	Non-controlling interest	Total
		EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT							
		U.S. dollars in thousands							
BALANCE AT 1 JANUARY 2012		16,597	97,356	12,356	266,692	(2,981)	390,020	-	390,020
Comprehensive income:									
Income for the year		-	-	-	51,570	-	51,570	410	51,980
Other comprehensive income	2c	-	-	4,393	(4,756)	-	(363)	-	(363)
Total comprehensive income for the year		-	-	4,393	46,814	-	51,207	410	51,617
Plan for allotment of Company shares to employees of subsidiary:									
Purchase of Company shares by subsidiary	2r	-	-	-	-	(1,330)	(1,330)	-	(1,330)
Receipts in respect of allotment of Company shares to employees	12b	-	(846)	-	-	1,268	422	-	422
Allotment of shares and options to senior employees- Recognition of compensation related to employee stock and option grants	12b	-	1,553	-	-	-	1,553	-	1,553
Proceeds from issuance of shares to senior employees		116	4,036	-	-	-	4,152	-	4,152
Dividend paid	12c	-	-	-	(3,029)	-	(3,029)	-	(3,029)
		16,713	102,099	16,749	310,477	(3,043)	442,995	410	443,405
Non-controlling interest from business combination		-	-	-	-	-	-	1,825	1,825
BALANCE AT 31 DECEMBER 2012		16,713	102,099	16,749	310,477	(3,043)	442,995	2,235	445,230

(Continued) - 2

FRUTAROM INDUSTRIES LTD.

CONSODLIATED STATEMENTS OF CHANGES IN EQUITY

	Note	Ordinary shares	Other capital surplus	Translation differences	Retained earnings	Cost of company shares held by the company	Total attributed to owners of parent company	Non-controlling interest	Total
		EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT							
		U.S. dollars in thousands							
BALANCE AT 1 JANUARY 2013		16,713	102,099	16,749	310,477	(3,043)	442,995	2,235	445,230
Comprehensive income:									
Income for the year		-	-	-	63,129	-	63,129	492	63,621
Other comprehensive income	2c	-	-	10,547	2,153	-	12,700	75	12,775
Total comprehensive income for the year		-	-	10,547	65,282	-	75,829	567	76,396
Plan for allotment of Company shares to employees of subsidiary:									
Purchase of Company shares by subsidiary	2r	-	-	-	-	(851)	(851)	-	(851)
Receipts in respect of allotment of Company shares to employees	12b	-	(1,276)	-	-	1,913	637	-	637
Allotment of shares and options to senior employees- Recognition of compensation related to employee stock and option grants	12b	-	1,510	-	-	-	1,510	-	1,510
Proceeds from issuance of shares to senior employees		68	1,960	-	-	-	2,028	-	2,028
Dividend paid to the non-controlling interests in subsidiary		-	-	-	-	-	-	(97)	(97)
Dividend paid	12c	-	-	-	(3,892)	-	(3,892)	-	(3,892)
		16,781	104,293	27,296	371,867	(1,981)	518,256	2,705	520,961
Non-controlling interest from business combination		-	-	-	-	-	-	98	98
BALANCE AT 31 DECEMBER 2013		16,781	104,293	27,296	371,867	(1,981)	518,256	2,803	521,059

The accompanying notes are an integral part of these financial statements.

(Concluded) - 3

FRUTAROM INDUSTRIES LTD.

CONSODLIATED STATEMENTS OF CHANGES IN EQUITY

	Note	Ordinary shares	Other capital surplus	Translation differences	Retained earnings	Company shares held by the company	Cost of owners of parent company	Total attributed to Non-controlling interest	Total
		EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT							
		U.S. dollars in thousands							
BALANCE AT 1 JANUARY 2014		16,781	104,293	27,296	371,867	(1,981)	518,256	2,803	521,059
Comprehensive income:									
Income for the year		-	-	-	86,654	-	86,654	962	87,616
Other comprehensive income	2c	-	-	(75,455)	(8,156)	-	(83,611)	(49)	(83,660)
Total comprehensive income for the year		-	-	(75,455)	78,498	-	3,043	913	3,956
Plan for allotment of Company shares to employees of subsidiary:									
Purchase of Company shares by subsidiary	2r	-	-	-	-	(1,131)	(1,131)	-	(1,131)
Receipts in respect of allotment of Company shares to employees	12b	-	(350)	-	-	525	175	-	175
Allotment of shares and options to senior employees- Recognition of compensation related to employee stock and option grants	12b	-	1,480	-	-	-	1,480	-	1,480
Proceeds from issuance of shares to senior employees		41	1,241	-	-	-	1,282	-	1,282
Dividend paid to the non-controlling interests in subsidiary		-	-	-	-	-	-	(90)	(90)
Dividend paid	12c	-	-	-	(4,712)	-	(4,712)	-	(4,712)
		41	2,371	-	(4,712)	(606)	(2,906)	(90)	(2,996)
BALANCE AT 31 DECEMBER 2014		16,822	106,664	(48,159)	445,653	(2,587)	518,393	3,626	522,019

The accompanying notes are an integral part of these financial statements.

FRUTAROM INDUSTRIES LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Note	2014	2013	2012
		Year ended 31 December		
		U.S. dollars in thousands		
CASH FLOWS FROM OPERATING ACTIVITIES:				
Cash generated from operations (see Appendix)		99,201	98,493	104,774
Income tax paid - net		(18,358)	(9,802)	(13,563)
Net cash provided by operating activities		80,843	88,691	91,211
CASH FLOWS FROM INVESTING ACTIVITIES:				
Purchase of property, plant and equipment		(21,392)	(20,111)	(12,558)
Purchase of intangibles		(1,197)	(868)	(2,284)
Interest received		493	276	195
Acquisition of subsidiaries - net of cash acquired	5	(34,723)	(114,620)	(75,280)
Proceeds from sale of property		800	264	271
Net cash used in investing activities		(56,019)	(135,059)	(89,656)
CASH FLOWS FROM FINANCING ACTIVITIES:				
Dividend paid to the non-controlling interests in subsidiary		(90)	(97)	-
Receipts from senior employees in respect of allotment of shares		1,282	2,028	4,152
Interest paid		(2,414)	(3,456)	(5,553)
Receipt of long-term bank loans		32,892	45,693	131,231
Repayment of long-term bank loans		(52,214)	(41,750)	(116,802)
Receipt of short-term bank loans and credit - net		14,980	52,809	7,319
Purchase of Company shares by subsidiary – net of receipts in respect of the Shares		(956)	(214)	(908)
Dividend paid		(4,712)	(3,892)	(3,029)
Net cash provided by financing activities		(11,232)	51,121	16,410
INCREASE IN CASH, CASH EQUIVALENTS AND BANK CREDIT		13,592	4,753	17,965
Balance of cash and cash equivalents and bank credit at beginning of year		57,612	53,933	36,472
losses from exchange differences on cash, cash equivalents and bank credit		(7,229)	(1,074)	(504)
BALANCE OF CASH, CASH EQUIVALENTS AND BANK CREIDT AT END OF YEAR		63,975	57,612	53,933

The accompanying notes are an integral part of these financial statements.

FRUTAROM INDUSTRIES LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

APPENDIX TO CONDENSED CONSOLIDATED STATEMENT CASH FLOWS

	Year ended December 31		
	2014	**2013**	**2012**
	U.S. dollars in thousands		
Cash generated from operations:			
Income before tax	108,835	79,229	65,608
Adjustments required to reflect the cash flows from operating activities:			
Depreciation and amortization	30,551	27,693	26,012
Recognition of compensation related to employee stock and option grants	1,480	1,510	1,553
Liability for employee rights upon retirement - net	586	166	(655)
Loss (gain) from sale and write-off of fixed assets and other assets	(147)	(150)	92
Erosion of loans	(1,336)	1,212	1,003
Interest paid - net	1,921	3,180	5,358
Change in fair value of financial instruments	-	-	289
Change in put option value	(4,108)	-	-
Income from bargain purchase	-	-	(1,729)
	28,947	33,611	31,923
Operating changes in working capital:			
Decrease (increase) in accounts receivable:			
Trade	(10,937)	(8,966)	(1,712)
Other	1,868	(848)	(206)
Decrease in other long-term receivables	80	258	136
Increase (decrease) in accounts payable:			
Trade	1,911	3,432	1,506
Other	(5,922)	(2,999)	3,772
decrease in other long-term payables	(230)	(117)	(379)
Decrease (increase) in inventories	(25,351)	(5,107)	4,126
	(38,581)	(14,347)	7,243
Cash flows from operating activities	99,201	98,493	104,774

NOTE 1 – GENERAL

Information on the activities of Frutarom Industries Ltd. and its subsidiaries (hereafter - the "Group").

Frutarom Industries Ltd. (hereafter – the Company) is a global company, founded in 1933. The Company operates through an Israeli subsidiary (hereafter - Frutarom Ltd.) and the companies under its control. The Group has two main operations: the Flavors activity and the Fine Ingredients activity, which are considered as core business by management.
In addition, the Company imports and markets raw materials produced by others as part of its services and strive to provide complete solutions for customers. This activity is presented as part of trade and marketing operations.
The Group develops, manufactures, markets and sells flavors and fine ingredients used by food and beverage producers, pharma-nutraceutical, flavors and fragrances, and personal care and cosmetics products as well as other products. The Group sells its products in more than 150 countries to more than 16,000 clients. The Group has production facilities in Europe, North America, Latin America, Israel and Asia; The group has 42 research and development laboratories and it sells and markets its products principally through its 73 sales and marketing offices. Segment information for the reporting years is presented as part of Note 6.
The Company is a limited liability company incorporated and domiciled in Israel. The address of its registered office is 25 Heshaish St., Haifa Bay. The Company's controlling shareholder is ICC Industries Inc.

The Company's shares have been listed on the Tel-Aviv Stock Exchange (the "TASE") since 1996. Since February 2005, Company shares are also listed through Global Depository Receipts on the official list of the London Stock Exchange (the "LSE").

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

a. Basis of Preparation:

1) The Group's financial statements as of 31 December 2014 and 2013 and for each of the three years in the period ended 31 December 2014, are in compliance with International Financial Reporting Standards (hereafter – IFRS) and interpretations to IFRS issued by the International Financial Reporting Interpretations Committee (IFRIC) and include the additional disclosure required under the Securities Regulations (Annual Financial Statements), 2010.

   The significant accounting policies described below have been applied consistently in relation to all the years presented, unless otherwise stated.

   The financial statements have been prepared under the historical cost convention, subject to adjustments in respect of revaluation of amounts funded for severance pay, financial assets at fair value through profit or loss presented at fair value.

   The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in (Note 4). Actual results could differ significantly from those estimates and assumptions.

2) The period of the Group's operating cycle is 12 months.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

3) The Group analyses the expenses recognized in the income statements using the classification method based on the functional category to which the expense belongs.

b. Principles of Consolidation

Subsidiaries are all entities (including structured entities) over which the group has control. The group controls an entity when the group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the group. They are deconsolidated from the date that control ceases

The group applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary (hereafter – the acquired company) is the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the Group.
The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred.
Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination (except for certain exceptional items specified in IFRS 3 – "Business Combinations") (as amended), hereafter – IFRS 3R) are measured initially at their fair values at the acquisition date.

Any contingent consideration accrued to the Group as part of a business combination is measured at fair value at the date of business acquisition. Subsequent changes to the fair value of the contingent consideration that is deemed to be an asset or liability is recognized in accordance with IAS 39 "Financial Instruments" either in profit or loss or as a change to other comprehensive income. Contingent consideration that is classified as equity is not re-measured, and its subsequent settlement is accounted for within equity.

The excess of the overall amount of the transferred consideration, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the Group's share of the identifiable net assets acquired and the liabilities assumed is recorded as goodwill –(see also f(1) below).
In cases were the net amount at acquisition date of the identifiable assets acquired and of the liabilities assumed exceeds the overall consideration that was transferred, the amount of non controlling interest in the acquiree and the fair value as of date of acquisition of any previous equity interest in the acquiree as above, the difference is recognized directly in income or loss at date of acquisition.

Inter-company transactions, balances, including income, expenses and dividends on transactions between group companies are eliminated. Profits and losses resulting from inter-company transactions that are recognized in assets (in respect of inventory and fixed assets) are also eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

c. Translation of Foreign Currency Balances and Transactions:

1) Functional and Presentation Currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which that entity operates (the "Functional Currency"). The consolidated financial statements are presented in U.S. dollars, which is the Company's functional and presentation currency.

2) Transactions and balances.

Foreign currency transactions in currencies different from the functional currency (hereafter – foreign currency) are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are re-measured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are attributed to income or loss.
Gains and losses arising from changes in exchange rates are presented in the statement of income among "financial expenses".

3) Translation of Financial Statement of Group Companies

The results and financial position of all the Company's entities (none of which has the currency of hyperinflationary economy) that have a Functional Currency different from the presentation currency are translated into the presentation currency as follows:

(a) Assets and liabilities for each statement of financial position presented are translated at the closing rate at the date of that statement of financial position;
(b) Income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates: in which case income and expenses are translated at the rate on the dates of the transactions);
(c) All resulting exchange differences are recognized among other comprehensive income.

On consolidation of the financial statements, exchange differences arising from the translation of the net investment in foreign operations and from loans and other currency instruments designated to serve as hedges to those investments are carried to other comprehensive income. When a foreign operation is partially disposed of or sold, exchange differences that were recorded in other comprehensive income are recognized in the statement of income as part of the gain or loss on realization or sale.

Goodwill and fair value adjustments arising on the acquisition of foreign operations are treated as assets and liabilities of the foreign operations and translated at the closing rate. Exchange differences arising from translation as above are recognized in other comprehensive income.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

4) Information regarding exchange rates, based on data published by the Bank of Israel:

	NIS	Pound Sterling	Euro	Swiss Franc	Ruble
Exchange rate as of December 31:					
2014	3.89	0.64	0.82	0.99	59.67
2013	3.47	0.60	0.73	0.89	32.79
2012	3.73	0.62	0.76	0.92	30.44
Increase (decrease) of the dollar: during the year	%	%	%	%	%
2014	12.0	6.1	13.4	11.1	82.0
2013	(7.0)	(2.2)	(4.3)	(2.8)	7.7
2012	(2.3)	(4.6)	(1.9)	(2.7)	(5.1)

	NIS	Pound Sterling	Euro	Swiss Franc	Ruble
Average exchange rate during the year:					
2014	3.58	0.61	0.75	0.91	38.96
2013	3.61	0.64	0.75	0.93	31.84
2012	3.86	0.63	0.78	0.94	30.99
Increase (decrease) during of the dollar during the year:	%	%	%	%	
2014	(0.9)	(5.0)	(0.1)	(1.4)	19.6
2013	(6.3)	1.3	(3.3)	(1.2)	2.7
2012	7.8	1.2	8.3	5.9	5.7

d. Segment Reporting (see also note 1)

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker in the Group, who is responsible for allocating resources and assessing performance of the operating segments.

The Group is organized and managed on a worldwide basis in two major operating activities: Flavors and the Fine Ingredients. Another operation is Trade and Marketing. Each activity constitutes a segment.

e. Property, Plant and Equipment:

The cost of a property, plant and equipment item is recognized as an assets only if: (a) it is probable that the future economic benefits associated with the item will flow to the Group and (b) the cost of the item can be measured reliably.

Property, plant and equipment is stated at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items and only when the two criteria mentioned above for recognition as assets are met.

The carrying amount of a replaced part is derecognized. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

The cost of a property, plant and equipment item includes:

(a) Its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates.

(b) Any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably.

Depreciation and impairment of property, plant and equipment are recognized in the income statement.

Land owned by the Group is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost less their residual values over their estimated useful lives, as follows:

	Percentage of Annual Depreciation
Buildings and land under financial lease	2-4
Machinery and equipment	5-10
Vehicles and lifting equipment	15-20
Computers	20-33
Office furniture and equipment	6-20
Leasehold improvements	See below

Leasehold improvements are amortized by the straight-line method over the terms of the lease, which are shorter than the estimated useful life of the improvements.

The asset's residual values, the depreciation method and useful lives are reviewed, and adjusted if appropriate, at least once a year.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2g).

Gains or losses on disposals are determined by comparing proceeds with carrying amount. These are included in the statement of income among "other income - net".

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

f. Intangible Assets:

1) The overall amount of goodwill arising on acquisition of a subsidiary, associated company or a proportionately consolidated company represents the excess of the consideration transferred in respect of acquisition of a subsidiary over the net amount as of acquisition date of the identifiable assets acquired and the liabilities assumed. Goodwill on acquisitions of subsidiaries is included in ‘intangible assets’.
For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the cash generating units (CGUs), or groups of CGUs that is expected to benefit from the synergies of the combination. Each unit or group of units to which the goodwill is allocated represents the lowest level within the entity at which the goodwill is monitored for internal management purposes and which is not larger than an operating segment (before aggregation) (see also g. below).
Impairment reviews of CGUs (or groups of CGUs) are undertaken annually and whenever there is any indication of impairment of CGU or group of CGUs. The carrying value of the CGU (or group of CGUs) is compared to the recoverable amount, which is the higher of value in use and the fair value less costs to sell.
Any impairment loss is allocated to write-down the carrying amount of the CGU's assets (or CGUs) in the following order: first, the write down of any goodwill allocated to a cash generating unit (or a group of CGUs); and afterwards to the remaining assets of the CGU or (group of CGUs) on a proportionate basis using the carrying amounts of each asset of the CGU (or group of CGUs).
Any impairment is recognized immediately as an expense and is not subsequently reversed. During the reported year, Company's management decided to consolidate the UK savory cash generating unit with the German savory cash generating unit in light of the actual merge that was done during the year. in order to continue exploiting commercial and operational synergies, Company management is considering consolidating a number of additional cash generating unit In 2015.
.

2) Product formulas acquired as part of a business combination transaction are initially recorded at fair value and amortized on a straight-line basis over their useful lives (10-20 years); (mainly 20 years).

3) Customer relationships acquired in a business combination are measured at fair value at the acquisition date. The customer relations have a finite useful life and are carried at the recognized amount less accumulated amortization. Amortization is calculated using the straight-line method over the expected life of the customer relationship (7-10 years).

4) Separately acquired trademarks and licenses are shown at historical cost. Trademarks and licenses acquired in a business combination are recognized at fair value at the acquisition date. Trademarks and licenses have a definite useful life and are presented at cost less accumulated amortization. Amortization is calculated using the straight-line method to allocate the cost of trademarks over their estimated useful lives (20 years).

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

5) Computer software

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring to use the specific software licenses. These costs are amortized over their estimated useful lives (3-5 years) using the straight line method.
Costs associated with maintaining computer software programmes are recognized as an expense as incurred. Costs that are directly associated with the development of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognized as intangible assets. Costs include the employee costs incurred as a result of developing software and an appropriate portion of relevant overheads.
Computer software development costs recognized as assets are amortized over their estimated useful lives using the straight line method (3-5 years) commencing the point in time when the asset is available for use, i.e., it is in the location and condition necessary for it to be capable of operating in the manner intended by management.

6) Research and Development

Research expenses are accounted for as expenses as incurred. Cost incurred in respect of development projects (attributable to the design and testing of new or improved products) are recognized as intangible assets when the following criteria are met:

- It is technically feasible to complete the intangible assets so that it will be available for use;
- Management intends to complete the intangible asset and use it or sell it;
- There is an ability to use or sell the intangible asset;
- It can be demonstrated how the software product will generate probable future economic benefits;
- Adequate technical, financial and other resources to complete the development and to use or sell the intangible asset are available; and
- The expenditure attributable to the intangible asset during its development can be reliably measured.

Other development costs that do not qualify for recognition as assets are recognized as cost as incurred. Development costs previously recognized as an expense are not recognized as an asset on a subsequent period. Capitalized development costs are presented as intangible assets and amortized as from the time the asset is available for use, i.e., when it is in the location and condition necessary for it to be capable of operating in the manner intended by management through its useful life in accordance with the straight-line method.
The Group fully recognized the R&D expenses as incurred.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

g. Impairment of non-financial assets

Assets that have an indefinite useful life, such as goodwill or intangibles that are not yet available for use are not subject to amortization and are tested annually for impairment or more often if events have occurred or changes in circumstances indicate that the carrying amount may not be recoverable.
Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.
An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets, other than goodwill, that were subject to impairment are reviewed for possible reversal of the impairment recognized in respect thereof at each statement of financial position date.

h. Government Grants

The group's research and development activities are supported in some of the countries in which it operates, and in Israel through the Israel Chief Scientist in the Ministry of Industry, Commerce and Labour (hereinafter - the OCS) by way of grants.

Grants from the government are recognized at their fair value where there is a reasonable assurance that the grant will be received and the Group will comply with all attached conditions.

Government grants relating to costs are recognized in the income statement on a systematic basis over the periods in which the Group recognizes the relating costs (the costs that the grants are intended to compensate).

i. Financial assets:

1) Classification

The Group classifies its financial assets in the following categories: Financial assets at fair value through profit or loss and loans and receivables. The classification depends on the purpose for which the financial assets were acquired. Group management determines the classification of its financial assets at initial recognition.

a) Financial assets at fair value through profit or loss

This category includes two sub-categories: financial assets held for trade and financial assets designated at fair value through profit or loss. A financial asset is classified into this category if it was acquired principally for the purpose of selling in the short term or if was designated to this category by management. Assets in this category are classified as current assets if expected to be settled within 12 months, otherwise they are classified as non-current.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

b) Receivable

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the statement of financial position date. These are classified as non-current assets. Receivables of the Group are classified as "accounts receivable" in the statement of financial position (Note 2k below).

2) Recognition and measurement

Regular purchases and sales of financial assets are recognized on the settlement date, which is the date on which the asset is delivered to the Group or delivered by the Group. Investments are initially recognized at fair value plus transaction costs for all financial assets not measured at fair value through profit or loss. Financial assets measured at fair value through profit or loss, are initially recognized at fair value, and transaction costs are expensed in the statement of income. Financial assets are derecognized when the rights to receive cash flows there from have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are measured in subsequent periods at amortized cost using the effective interest method.

Gains or losses that stem from changes in the fair value of financial assets at fair value through profit or loss are presented in statement of income under "financial expenses - net" in the period in which they incurred. Dividend income from financial assets at fair value through profit or loss are recognized in statement of income under "other income - net" when the group is eligible to these payments.

3) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

4) Impairment of financial assets

Financial assets are presented at amortized cost.

The Group assesses at the each statement of financial position date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a ‘loss event’) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The criteria that the Group uses to determine that there is objective evidence of an impairment of a financial assets or group of financial assets include observable: information that came to the attention of the Group in connection with the following loss events:

- Significant financial difficulty of the issuer or obligor;
- breach of contract, such as a default or delinquency in interest or principal payments;
- The Group, for economic or legal reasons relating to the borrower’s financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;
- It becomes probable that the borrower will enter bankruptcy or other financial reorganization;
- The disappearance of an active market for that financial asset because of financial difficulties;
- Observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the portfolio, including:
  - (i) Adverse changes in the payment status of borrowers in the portfolio; or
  - (ii) National or local economic conditions that correlate with defaults on the assets in the portfolio.

Where objective evidence for impairment exists, the amount of the loss is measured as the difference between the asset’s carrying amount of the financial assets and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset’s original effective interest rate (i.e., the effective interest rate computed for the asset upon initial recognition). The asset’s carrying amount is reduced and the amount of the loss is recognized in the statement of income.

If the amount of impairment loss in a subsequent period decreases, and this decrease may be attributed to an objective event that took place after the impairment was recognized (like improved credit rating of the borrower), reversing the previously recognized impairment loss is recorded in income statements.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

j. Inventories

Inventories are measured at the lower of cost or net realizable value. Raw material cost is determined using the "moving average" method.

The cost of finished goods and work in progress comprises raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity) but excludes capitalization of borrowing costs.

Net realizable value is the estimated selling price in the ordinary course of business, less the applicable and variable selling expenses.

k. Trade Receivables

Trade receivables are amounts due from customers for merchandise sold or services performed in the ordinary course of business. If collection is expected in one year or less they are classified as current assets. If not, they are classified as non-current assets.

Trade receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less provision for doubtful accounts (hereafter – "provision for impairment" or "provision for doubtful accounts"). As to the way the impairment provision is determined and accounting treatment applied thereto subsequently see i4) below.

l. Cash and Cash Equivalents

Cash and cash equivalents include cash in hand, short-term bank deposits and other highly liquid short-term investments, the maturity of which does not exceed three months, bank overdrafts (repayable upon demand).

m. Share Capital

Ordinary shares of the Company are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown as a deduction, net of tax, from the proceeds of issuance.

Where any Group company purchases the Company’s equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the company’s equity holders until the shares are cancelled or reissued. Where such shares are subsequently reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects are included in equity. Any difference between the cost of acquisition of the treasury shares and the consideration is carried to premium on shares.

n. Trade Payables

Trade payables are obligations of the Group to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

If not, they are classified as non-current liabilities.
Trade payables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

o. Loans

Loans are recognized initially at their fair value, net of transaction costs incurred. Loans are subsequently measured at amortized cost; any difference between the consideration (net of transaction costs) and the redemption value is recognized in the statement of income over the period of the loan using the effective interest method.
Loans are classified as current liabilities unless the Group has an unconditional right to defer settlement of the loans for at least 12 months after the end of the reporting period, in which case they are classified as non-current liabilities.

p. Current and Deferred Income Taxes

The tax expenses for the reported years comprise of current and deferred tax. Tax is recognized in the statement of income, except for taxes related to equity and other comprehensive income items.

The current income tax charge is calculated on basis of the tax laws enacted or substantially enacted at the statement of financial position date in the countries where the Company and the subsidiaries operate and generate taxable income. Management periodically evaluates tax issues related to its taxable income, based on relevant tax law, and makes provisions in accordance with the amounts payable to the Income Tax Authorities.

Deferred income tax is recognized using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Nevertheless, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affect neither accounting nor taxable income.

Deferred income tax assets are recognized to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized. The amount of deferred income taxes is determined using tax rates (and laws) that have been enacted or substantially enacted by the statement of financial position date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax is not calculated on temporary differences arising on investments in subsidiaries, as long as the timing of reversal of the differences is controlled by the Group and it is expected that no such reversal will take place in the foreseeable future.

The group recognizes deferred income tax assets in respect of temporary differences deductible for tax purposes only if it is expected that the temporary difference is revered in the foreseeable future and to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

Deferred income tax assets and liabilities are offset only if:

- There is a legally enforceable right to offset current tax assets against current tax liabilities; and

- When the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

As stated in Note 13c, upon distribution of dividends from tax-exempt income of "approved enterprises" or "benefited enterprises", the amount distributed will be subject to tax at the rate that would have been applicable had the company not been exempted from payment thereof. The amount of the related tax is charged as an expense in the statement of comprehensive income, when such dividend is distributed.

q. Employee Benefits:

1) Pension Obligations and retirement benefits

The companies in the group operate a number of post-employment employee benefit plans, including defined benefit and defined contribution plans.

A defined contribution plan is a pension plan under which the group pays fixed contributions into a separate entity. The group has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

A defined benefit plan is a pension plan that is not a defined contribution plan.

The companies in the group operate a number of pension plans. The plans are funded through payments to insurance companies or pension funds that are managed in trust.

According to their terms, those pension plans satisfy the above definition of a defined contribution plan.

According to labor laws and agreements in Israel and the practices of the companies in the Group, Group companies are obligated to pay retirement benefits to employees dismissed or retiring in certain circumstances.

According to the obligation of group companies to employees who participate in a defined benefit plan, the amounts of benefits those employees are entitled to upon retirement are based on the number of years of services and the last monthly salary.

The obligation of the group companies to all other employees is a defined contribution plan, in which regular contributions are made to a separate and independent entity, and the companies of the Group have no legal or constructive liability to make any further payments if the assets of the funds are insufficient to pay all employees the benefits for work services in the current and past periods.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

The total retirement benefit obligation presented in the statement of financial position is the present value of defined benefit contribution as of the date of financial position, less the fair value of plan assets. The defined contributions benefit is measured on an annual basis by an actuary using the projected unit credit method.

The present value of the liability is determined by discounting expected future cash flows (after taking into account the expected rate of payroll hikes) based on the interest rate of government/corporate bonds denominated in the currency in which the benefits will be paid and whose terms to maturity approximate the term of retirement benefit obligation.

According to IAS 19 "Employee Benefits", the discount rate used for calculating the actuarial obligation is determined by using the market return of high-quality corporate bonds on the date of the statement of financial position. However, IAS 19 indicates that in countries where there is no deep market in such bonds, the market rates on government bonds are used.

The group recognizes remeasurements of net obligations (the asset) for defined benefit plan to other comprehensive income in the period in which they incurred. Those remeasurements are created as a result of changes in actuary assumptions, difference between past assumptions and actual results and differences between plan assets return and the amounts included in net interest on net liabilities (the asset) for defined benefit.

Past-service costs are recognized immediately in income.

Amount funded for severance benefits are measured at fair value. The amounts funded are plan assets as defined by IAS 19, and therefore were offset from the balance of retirement benefit obligation for presentation purposes in the statement of financial position.

As discussed above, the group purchase insurance policies and make contributions to pension and severance pay funds to fund its obligation under defined contribution plan. The group has no further payment obligations once the contributions have been paid. The contributions are defined as an expense for employee benefits concurrently to receiving services from employees that entitle them for contributions. Prepaid contributions are recognized as an asset to the extent that a cash refund or a reduction in the future payments is available.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

2) Vacation and Recreation Fees

Under the law in various countries, employee is entitled for vacation days and recreation fees (in Israel), both computed on an annual basis. The entitlement is based on the period of employment. The Group records a liability and an expense in respect of vacation and recreation fees, based on the benefit accumulated for each employee.

3) Bonus plans

Some of the Group's employees are entitled to receive an annual bonus in accordance with the bonuses plan determined by Group management for that year. The Group provides for payment of the bonus in accordance with meeting the targets of the plan and in accordance with Group's estimate as to the total amount of bonuses to be paid to employees.

r. Share-Based Compensation

The group operates a number of equity-settled, share-based compensation plans, under which the entity receives services from employees as consideration for equity instruments (options) of the group. The fair value of the employee services received in exchange for the grant of the options is recognized as an expense. The total amount to be expensed is determined by reference to the fair value of the options granted:

- including any market performance conditions (for example, an entity's share price);
- Excluding the impact of any service and non-market performance vesting conditions (for example, profitability, sales growth targets and remaining an employee of the entity over a specified time period); and
- Including the impact of any non-vesting conditions (for example, the requirement for employees to save).

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

s. Provisions

Provisions are recognized when the Group has a present legal or constructive obligation as a result of past events and it is probable that an outflow of resources will be required to settle the obligation and it is possible to prepare a reliable estimation of the amount of liability.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole.

Provisions are measured at the present value of the cash flow expected to be required to settle the obligation using a pre-tax discount rate that reflects current market assessments of the time value of money and the risk specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

t. Revenue Recognition Policy

Revenue is measured at the fair value of the consideration received or receivable for the sale of goods in the ordinary course of business. Revenue is shown net of value-added tax, returns, rebates and discounts and after eliminating sales within the Group.

Revenues from sale of goods are recognized by the Group when all of the following conditions are met:

(a) The significant risks and rewards of ownership of the goods have been transferred by the Group to the buyer;
(b) The group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold.
(c) The amount of revenues can be reliably measured.
(d) It is probable that future economic benefit relating to the transaction will flow to the Group; and
(e) The costs incurred or to be incurred in respect of the transaction can be measured reliably.

The amount of revenue is not considered to be reliably measurable until all contingencies relating to the transaction have been resolved. The Group bases its estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

The products are occasionally sold with volume discounts; customers have a right to return faulty products. Sales are recorded based on the selling price, net of the estimated volume discounts and returns at the time of sale. Accumulated experience is used to estimate and provide for the discounts and returns. The volume discounts are assessed based on anticipated annual purchases. No element of financing is present as the sales are made with an average credit term, which is not higher than the market practice.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

u. Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.
Long term lease contracts for lease of land from the Israel Land Administration and from other countries are presented among fixed assets.

v. Earnings per Share

Basic:

The computation of basic earnings per share is based, as a general rule, on the profit attributable to holders of ordinary Company shares divided by the weighted average number of ordinary shares in issue during the period, excluding Company shares held by group subsidiaries (Notes 2m).

Fully Diluted:

When calculating the diluted earnings per share, the Group adds to the average number of shares outstanding that was used to calculate the basic earnings per share also the weighted average of the number of shares to be issued assuming the all shares that have a potentially dilutive effect would be converted into shares. The potential shares, as above are only taken into account in cases where their effect is dilutive (reducing the earnings per share or increasing the loss per share).

The weighted average number of shares used in calculating Basic and Diluted earnings per share is as follows:

	Basic	**Diluted**
	In thousands	**In thousands**
Year end 31 December:		
2014	58,228	59,078
2013	57,976	58,559
2012	57,344	57,613

w. Dividends

Dividend distribution to the Company's owners is recognized as a liability in the Group's statement of financial position on the date on which the dividends are approved by the Group’s Board of Directors. Dividend paid includes an erosion component (from date of approval of dividend through date of payment thereof).

x. New International Financial Reporting Standards, Amendments to Standards and New interpretations

Standards and amendments to existing standards, which are effective and mandatory for reporting periods starting on January 1, 2014:

a) Amendment to IFRS 2 "Share-Based Payment" (hereinafter - IFRS 2 Amendment)
IFRS 2 Amendment was published as part of the IASB's 2010-2012 cycle of the annual improvements project. The amendment clarifies the definition of a "vesting condition", "market conditions" and separately defines "performance condition" and "service condition".

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

The amendment is effective for share-based payment transactions for which the grant date is on or after July 1, 2014. The first-time adoption of the Amendment had no material impact on the consolidated financial statements of the Group.

b) IFRS 3 "Business Combinations" (hereinafter - IFRS 3 Amendment)

IFRS 3 Amendment was published as part of the IASB's 2010-2012 cycle of the annual improvements project. The Amendment clarifies that all non-equity contingent consideration is measured at fair value, with changes in fair value recognized in profit and loss, either if the contingent consideration meets the definition of a financial instrument or not.

The amendment is effective retrospectively for business combinations where the acquisition date is on or after July 1, 2014. The first-time adoption of the Amendment had no material impact on the consolidated financial statements of the Group.

Standards, amendments and interpretations to existing standards that are not yet effective and that the Group has not adopted early:

a) Amendment to IAS 32 "Offsetting Financial Assets and Financial Liabilities" (hereinafter - IAS 32 Amendment)

IAS 32 Amendment does not change the current model for offsetting financial assets and financial liabilities in IAS 32 "Financial Instruments: Presentation" (hereinafter: offsetting), but clarifies that the right to set-off must be available today – that is, it is not contingent on a future event. It also must be legally enforceable for all counterparties in the normal course of business, as well as in the event of default, insolvency or bankruptcy. IAS 32 Amendment also clarifies that grow settlement mechanisms may meet the offsetting criteria for net settlement.

The Group adopted IAS 32 Amendment retrospectively. The first-time adoption of the Amendment had no material impact on the consolidated financial statements of the Group.

b) IFRS 9 "Financial Instrument" (hereinafter - "IFRS 9" or "the standard")

IFRS 9 addresses the classification, measurement and recognition of financial assets and financial liabilities. The complete version of IFRS 9 was issued in July 2014. It replaces the guidance in IAS 39 "Financial Instrument: Recognition and Measurement" that relates to the classification and measurement of financial instruments. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortized cost, fair value through OCI and fair value through P&L. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in OCI not recycling.

The standard presents a new expected credit losses model that replaces the incurred loss impairment model used in IAS 39, which is based on the incurred loss model.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

For financial liabilities there were no changes to classification and measurement except for the recognition of changes in own credit risk in other comprehensive income.

IFRS 9 relaxes the requirements for hedge effectiveness by replacing the bright line hedge effectiveness tests. It requires an economic relationship between the hedged item and hedging instrument and for the ‘hedged ratio’ to be the same as the one management actually use for risk management purposes. Contemporaneous documentation is still required but is different to that currently prepared under IAS 39.

The standard is effective for accounting periods beginning on or after January 1, 2018. Early adoption is permitted. The group is assessing IFRS 9’s impact on its financial statements.

c) IFRS 15 "Revenue from Contracts with Customers" (hereinafter - IFRS 15)

IFRS 15 will replace after its first-time adoption the guidance on revenue recognition in current IFRSs.

The core principle of IFRS 15 is that revenue from contracts with customers should be recognized using the method that best depicts the transfer of control of goods and services to the customer, the amount of consideration that the entity expects to be entitled to in exchange for transferring promised goods or services to a customer.

IFRS 15 has a single model for revenue recognition, based on a five-step approach:

1. Identify the contract(s) with the customer
2. Identify the separate performance obligations in the contract
3. Determine the transaction price
4. Allocate the transaction price to separate performance obligations
5. Recognize revenue when (or as) each performance obligation is satisfied

IFRS 15 covers accounting for a variety of issues related to implementation of that model, including: recognition of contractual variable consideration, adjustment of contractual transaction price to reflect the time value of money, and cost of obtaining and fulfilling the contract.

The standard expands the disclosure requirements about revenue, and, among other things, requires quantitative and qualitative information about significant management judgments that were considered for determining the amount of revenue recognized.

The standard will be applied retrospectively for annual periods beginning on or after January 1, 2017, with some exceptions as provided in the transitional provisions of IFRS 15.

According to IFRS 15, early adoption is permitted. The Group is assessing the expected impact of IFRS 15 on its financial statements.

NOTE 3 - FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT:

a. Financial Risk Management

1) Financial Risk Factors

The Group's activities expose it to a variety of financial risks: market risk (including currency risk, fair value interest rate risk, cash flow interest rate risk and price risk), credit risk and liquidity risk. The Group's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Group's financial performance.

Risk management is carried out under policies approved by the board of directors and senior management. These policies cover specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of non-derivative financial instruments, and investment of excess liquidity. Group policies also cover areas such as cash management and raising short and long-term debt.

The Group's business is characterized by considerable dispersion. The Group produces tens of thousands of products intended for tens of thousands of customers throughout the world, using tens of thousands of raw materials purchased from a wide range of suppliers worldwide. As stated, the Group is not significantly dependent on any of its customers, products or suppliers.

Discussions on implementing the risk management policy as relates to currency exposure and interest are conducted by the Group's management once each quarter.

The Group does not use derivative financial instruments for its hedge or speculative purposes.

a) Market Risks:

1) Foreign Exchange Risk

The Group operates globally and is exposed to movements in foreign currencies affecting its net income and financial position, as expressed in U.S. dollars.
Transaction exposure arises because the equivalent amount in local currency paid or received in transactions denominated in foreign currencies may vary due to changes in exchange rates. Most Group entities produce their income primarily in the local currency. A significant amount of expenditures, especially for the purchase of goods for resale are in foreign currencies. Similarly, transaction exposure arises on net balances of financial assets held in foreign currencies. Since raw materials purchases for the Group's production are also conducted in various currencies, currency exposure is reduced.
The Group's subsidiaries manage this exposure locally. In addition, Group management monitors total global exposure of the Group.

Translation exposure arises from the consolidation of the Foreign Currency denominated financial statements of the Company's subsidiaries. The effect on the Group's consolidated comprehensive income is shown as a currency translation difference.

NOTE 3 – FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued):

The following table presents currency exposure in respect of balance denominated in currencies that are different than the functional currency of the reporting company and also the effect on income after taxes. At 31 December 2014, 2013 and 2012, if the currencies specified below had weakened/strengthened by 1% against the other functional currencies of group companies, with all other variables unchanged:

	31 December 2014			
	U.S. dollars in thousands			
	NIS	**Pound sterling**	**Euro**	**Swiss Franc**
Financial asset(liabilities), net	(2,586)	19	(21,354)	1,570
Gain (loss) from change:				
Impact of 1% weakening	26	*	214	(16)
Impact 1% strengthening	(26)	*	(214)	16

	31 December 2013			
	U.S. dollars in thousands			
	NIS	**Pound sterling**	**Euro**	**Swiss Franc**
Financial asset(liabilities), net	(1,373)	8	(39,241)	4,185
Gain (loss) from change:				
Impact of 1% weakening	11	*	315	(34)
Impact 1% strengthening	(11)	*	(315)	34

	31 December 2012			
	U.S. dollars in thousands			
	NIS	**Pound sterling**	**Euro**	**Swiss Franc**
Financial asset(liabilities), net	(3,713)	16	(23,922)	(21)
Gain (loss) from change:				
Impact of 1% weakening	29	*	189	*
Impact 1% strengthening	(29)	*	(189)	*

* Represents amounts lower than $1 thousand.

NOTE 3 – FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued):

2) Cash Flow Risk Relating to Interest Rates

Since on a current basis the Group does not have significant assets bearing interest, its revenues and operating cash flow are not dependent on changes in interest rates.

The Group's interest rate risk arises from long-term and short-term borrowings. Borrowings received at variable rates expose the Group to cash flow interest rate risk.

The Group analyses its interest rate exposure. Various scenarios are simulated taking into consideration refinancing, renewal of existing positions and alternative financing. Based on these scenarios, the Group calculates the impact on profit and loss of a defined interest rate shift. For each simulation, the same interest rate shift is used for all currencies. The scenarios are run only for liabilities that represent the major interest-bearing positions.

Based on the simulations performed, the impact on post tax profit for the year 2014 of a 0.1% shift in interest rate on loans would have been a change of $ 193 thousand (2013 - $ 171 thousand; 2012 - $124 thousand).

b) Credit Risk

Credit risk arises from the possibility that the counter-party to a transaction may be unable or unwilling to meet their obligations causing a financial loss to the Group.

Trade receivables are subject to a policy of active risk management, which focuses on the assessment of country risk, credit limits, ongoing credit evaluation and accounting monitoring procedures.

There are no significant concentrations within trade receivables of counter-party credit risk due to the large number of customers that the Group deals with and their wide geographical spread. Country risk limits and exposures are continuously monitored. Collateral is generally not required.

The provision for impairment of trade receivables is determined on basis of a periodic test of all amounts due.

The exposure of other financial assets and liabilities to credit risk is controlled by setting a policy for limiting credit exposure to counter-parties, continuously reviewing credit ratings, and limiting individual aggregate credit exposure accordingly.

c) Liquidity Risk

Group entities must have sufficient availability of cash to meet their obligations. Each company is responsible for its own cash management, including the short-term investment of cash surpluses and the raising of loans to cover cash deficits, subject to Group policies and to monitoring of Group management.

NOTE 3 – FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued):

The table presented below classifies the Group's financial liabilities into relevant maturity groupings based on the remaining period at 31 December 2014 to the contractual maturity date. Group entities do not have derivative financial liabilities. The amounts presented in the table represent the projected undiscounted cash flows.

	Less than 1 year	**Between 1 and 3 years**	**Between 3 and 5 years**
	U.S. dollars in thousands		
As of 31 December 2014:			
Borrowings	69,790	122,257	44,789
Liability for put option for the shareholders of a subsidiary	-	20,216	-
Accounts payable and accruals	107,151	3,233	3,096
	176,941	145,706	47,885
As of 31 December 2013:			
Borrowings	111,049	139,769	3,465
Liability for put option for the shareholders of a subsidiary	-	-	28,808
Accounts payable and accruals	111,238	5,850	-
	222,287	145,619	32,273

d) **Liability in respect of put option**

As part of the transaction for the acquisition of PTI, the former owner of Protein Technologies Ingredients ("PTI") was granted an option to sell to the company the remaining PTI shares, and the company has an option to buy those shares; (the price and the conditions of the call options is identical to the price of the put option). For further details about the option and the acquisition of PTI, see note 5e.

As of December 31, 2014, the amount of the option amounted to $ 20,966 thousands; the value of the liabilty was estimated in accordance with the average EBITDA to be achieved by PTI in the 12 quarters prior to the exercise of the option, multiplied by a multiplier of 6-7 and based on other performance factors. Due to the revaluation of the financial liability, the group recognized USD 4.7 million as finance expenses. The annual capitalization rate of the option is 1.65%.

The main unobservable data (Level 3) used by the company for the purpose of estimating the value of the option is the future EBITDA to be achieved. For the purpose of estimating the value of the liability for the option the company used PTI's current business results and the company forecast.
The fair value of the option is not materially different from than its value in the financial statements, since the discount rate remained unchanged.

b. Capital management

Group's objective is to maintain, as possible, stable capital structure. In the opinion of Group's management its current capital structure is stable. Consistent with others in the industry, the Group monitors capital, including others also, on the basis of the gearing ratio.

NOTE 3 – FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued):

This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings (including 'current and non-current borrowings' as shown in the consolidated statement of financial position) less cash and cash equivalents. Total capital is calculated as 'equity' as shown in the consolidated statement of financial position plus net debt.

The gearing ratios at 31 December 2014 and 2013 were as follows:

	2014	2013
	U.S. dollars in thousands	
Total borrowings (Note 9)	231,446	248,339
Less - cash and cash equivalents (Note 18)	(63,975)	(57,612)
Net debt	167,471	190,727
Total equity	522,019	521,059
Total capital	689,490	711,786
Gearing ratio	24.3%	26.8%

NOTE 4 – CRITICAL ACCOUNTING ESTIMATES AND ASSUMPTIONS

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will by definition, not necessarily be equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

a. Estimate of impairment of goodwill

The Group tests annually for impairment of goodwill, in accordance with the accounting policy states in note 2g. The recoverable amounts of cash-generating units have been determined based on value-in-use calculations. These calculations require the use of estimates (Note 8).

b. Taxes on income and deferred taxes

The Group is subject to income taxes in a large number of countries. Judgment is required in determining the worldwide provision for income taxes. The group is involved in transactions and computations whose final tax liabilities cannot be determined with certainty in the normal course of business. The Group recognizes liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due as a result of the tax audits. Where the final tax outcome of these matters, determined by tax authority is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax liabilities provisions in the period in which such determination is made.

The Group recognizes deferred tax assets and liabilities based on the differences between the financial statement carrying amounts and the tax bases of assets and liabilities. The Group regularly reviews its deferred tax assets for recoverability, based on historical taxable income, projected future taxable income, the expected timing of the reversals of existing temporary differences and the implementation of tax planning strategies. If the Group is unable to generate sufficient future taxable income, or if there is a material change in the actual effective tax rates or time period within which the underlying temporary differences become taxable or deductible, the Group could be required to eliminate a portion of the deferred tax asset resulting in an increase in its effective tax rate and an adverse impact on operating results.

NOTE 4 – CRITICAL ACCOUNTING ESTIMATES AND ASSUMPTIONS (continued):

c. Severance pay

The present value of the liabilities in respect of severance pay is dependent on several factors that are determined on an actuarial basis in accordance with various assumptions. The assumptions used in the calculation of the net cost (income) in respect of severance pay include, inter alia, the yields rate and the rate of discount. Changes in those assumptions shall influence the carrying amount of the assets and liabilities in respect of severance pay.
The assumption regarding the required rate of discount is determined by the external actuaries at the end of each year. This rate of discount shall be used in determining the estimated updated value of the future cash flows that would be required to cover the severance pay liabilities. The company uses the market of high-quality corporate bonds when this market available, when his not, government bonds is sufficient to serve as basis for determining the rate of discount. Therefore, in determining this rate the Group uses interest rate in the currency in which the benefits will be paid.
Other key assumptions relating to severance pay liabilities, such as future payroll raise and retirement rates are partially based on existing market conditions on that time and on past experience.

d. Provisions

Provision for legal liabilities are recorded in the books of accounts in accordance with Group management’s judgment (based on the opinion of its legal advisors) regarding the reasonability that the cash flows shall indeed by used to meet the liabilities, and on the basis of the estimate determined by the management regarding the present value of the expected cash outflows that would be required to meet the existing liabilities.

NOTE 5 – BUSINESS COMBINATIONS:

a. Acquisition of Savoury Flavours

On January 4, 2012, Frutarom signed, through a UK subsidiary, an agreement for the purchase of 100% of the share capital of UK company Savoury Flavours (Holding) Limited and its subsidiaries (hereafter – "Savoury Flavours") in consideration for $ 5.8 million (£ 3.8 million). In addition, the Company paid $ 0.4 million (£0.25 million) due to contingent consideration and working capital adjustment as of the day of the acquisition.

Founded in 1999, Savoury Flavours develops, manufactures, and markets savory taste solutions, including mainly flavors, seasoning compounds, marinades, and sauces, specializing in snacks and convenience foods. Savoury Flavours has a development, manufacturing, and marketing site in the United Kingdom, and a wide customer base including food manufacturers and private label manufacturers in the U.K. and in emerging markets.
In the 12 months ended December 31, 2011, Savoury Flavours' sales turnover total amounted $7.1 million.

NOTE 5 – BUSINESS COMBINATIONS (continued):

Savoury Flavours' production site is located close to EAFI's production site (savory operation that was acquired in 2011). Frutarom merged and combined the two operations as well as with integrated those operations into Frutarom's savory operations in the UK and all over the world. The geographic proximity, along with the two companies' complementary product portfolios and technologies, allow business synergies between Savory Flavours' and Frutarom's fast growing activities in savory foods categories in the UK and worldwide.

The transaction was financed using bank credit and was completed on the day the said agreement was signed.

The cost of acquisition was allocated to tangible assets, intangible assets and liabilities which were acquired based on their fair value at the time of the acquisition. The intangible assets recognized include product formulas in the total amount of £ 837 thousands ($ 1,291 thousands), customer relations in the total amount of £ 336 thousands ($ 518 thousands) and goodwill in the total amount of £ 2,492 thousands ($ 3,843 thousands).

Assets and liabilities of Savoury Flavours at the date of acquisition:

	Fair value
	U.S. dollars in thousands
Current assets:	
Accounts receivable:	
Trade	1,078
Inventory	990
Others	123
Non-current assets:	
Property, plant and equipment	170
Intangible assets:	
Product formula	1,291
Customer relations	518
Goodwill	3,843
Current liabilities :	
Accounts payable:	
Trade	(526)
Other	(865)
Non-current liabilities:	
Deferred income taxes	(447)
Other	(363)
	5,812

NOTE 5 – BUSINESS COMBINATIONS (continued):

b. Acquisition of Etol

In the first quarter of 2012, Frutarom purchased, through a Swiss subsidiary, app. 98% of the share capital of the public Slovenian company Etol in consideration for € 34.6 million. On May 8, 2012, Etol was delisted from the Slovenian Stock Exchange. On June 5, 2012 Frutarom has completed the acquisition of the remaining shares of Etol, So that the total cost of acquisition of all of Etol's shares amounted to approximately € 35.4 million ($ 45.7 million).

Together with its subsidiaries, Etol, founded in 1924, develops, manufactures and markets sweet and savory flavors, focusing on natural flavor products for the food and beverage industry. Etol also has great experience in development of fruit based flavors and products and Food Systems, specializing on local fruits of the region as well as extensive activating in the growing area of bases for beverages that plans to further invest in order to substantially expand its global activity.

Etol also has trade and marketing activities for products it does not manufacture, targeted for European countries, which will be integrated into the trade and marketing sector. Trade and marketing activities are not counted among Frutarom's core activities.

In the twelve months ended December 31, 2011, Etol group's consolidated sales turnover amounted to € 51.3 million ($ 71.4 million).

Etol has a sophisticated and innovative plant located on some 70 dunam of land east of Ljubljana in Slovenia. Etol’s products are sold to a wide customer base in Central and Eastern Europe and in emerging markets, including Russia, Poland, the Ukraine, Croatia, Serbia, Belarus, Hungary, Slovakia, Macedonia, the Czech Republic, Kazakhstan, Turkey and other emerging markets as well as developed countries such as the UK, Switzerland and Germany. Among Etol’s customers, leading food and beverage manufacturers in the countries it operates, including large multi-national food companies. The activitiese of Etol are synergetic with Frutarom’s activities.

Frutarom merge Etol's research and development, marketing and sales, logistics, procurement and manufacture with its own global operations, creating operational synergies and cross-selling. Frutarom also transferred manufacturing activities carried on in distant sites and/or in sites with high manufacturing costs; it utilized the logistic advantages of proximity to markets and maximized the competitive advantage by reducing production costs.

The consideration paid in cash amounted to $ 45,734 thousands (€ 35,387 thousands) and was fully funded by long-term bank credit.

The cost of acquisition was allocated to tangible assets, intangible assets and liabilities which were acquired based on their fair value at the time of the acquisition. The intangible assets recognized include product formulas in the total amount of € 2,472 thousands ($ 3,195 thousands), customer relations in the total amount of € 1,267 thousands ($ 1,637 thousands) and gain on a bargain purchase in the total amount of € 1,338 thousands ($ 1,729 thousands). The product formulas and customer relations are amortized over an economic useful life of 20 years and 10 years, respectively. The gain on a bargain purchase was recorded as a one-off income in the statement of income.

NOTE 5 – BUSINESS COMBINATIONS (continued):

Assets and liabilities of Etol at the date of acquisition:

	Fair value
	U.S. dollars in thousands
Current assets:	
Cash and cash equivalents	1,068
Accounts receivable:	
Trade	16,092
Inventory	10,435
Others	4,925
Non-current assets:	
Property, plant and equipment	38,647
Software	1,752
Other	629
Intangible assets:	
Product formula	3,195
Customer relations	1,637
Gain on a bargain purchase	(1,729)
Current liabilities :	
Accounts payable -	
Trade	(4,049)
Other	(2,988)
Deferred income taxes	(534)
Non-current liabilities	
Employee benefits	(2,144)
Long-term loans	(21,202)
	45,734

c. Acquisition of Mylner Industria E Comercio Ltda

On February 6, 2012 Frutarom signed, through a subsidiary, an agreement for the acquisition of 100% of the share capital of the Brazilian company Mylner Industria E Comercio (hereafter – "Mylner") and its parent company Vila Osorio Participacoes in consideration for $ 15.7 million (27.1 million Brazlian real). Frutarom also paid a total of 4.4 million Brazilian reals for the cash balance of Mylner out of which a total of 3.1 Brazilian real (capitalized value – 3 million Brazilian real) has not yet been paid for the acquisition date (of which 1.3 million Brazilian real were paid as of the end of the period) and used as security for the seller's indemnification liability in accordance with the purchase agreement, to be realized in installments over 3 years.

Mylnar, founded in 1974, develops, produces and markets sweet flavors for beverages and baked goods, and natural flavor products. Mylner has a modern development, production, and marketing site in the area of Sao Paulo, Brazil, including land for future expansion, and employs some 70 workers. Mylner's wide customer base includes leading food manufacturers mainly in Brazil, and in other developing countries in Latin America.

NOTE 5 – BUSINESS COMBINATIONS (continued):

In 2011, Mylner sales turnover amounted to $ 11.4 million (app. 19 million Brazilian real). The transaction was financed by a long term bank credit and was completed on the date of signing the agreement.

The cost of acquisition was allocated to tangible assets, intangible assets and liabilities which were acquired based on their fair value at the time of the acquisition. The intangible assets recognized include product formulas in the total amount of 2,948 thousands Brazilian real ($ 1,685 thousands), customer relations in the total amount of 2,707 thousands Brazilian real ($ 1,547 thousands) and goodwill in the total amount of 19,976 thousands Brazilian real ($ 11,415 thousands). The product formulas and customer relations are amortized over an economic useful life of 20 years and 10 years, respectively.

Assets and liabilities of Mylner at date of acquisition:

	Fair value
	U.S. dollars in thousands
Current assets:	
Cash and cash equivalents	2,542
Accounts receivable:	
Trade	680
Inventory	977
Non-current assets:	
Fixed assets	1,359
Intangible assets:	
Product formula	1,685
Customer relations	1,547
Goodwill	11,415
Current liabilities :	
Trade	(578)
Other	(5)
Short-term credit	(1,078)
Deferred income tax	(1,063)
Non-current liabilities	
Other	(1,025)
	16,456

d. Acquisition of JannDeRee (Pty) Limited

On May 2, 2013 the Company signed, through a subsidiary, an agreement for the acquisition of 100% of the share capital of the South African flavors company JannDeRee (Pty) Limited (hereafter – "JannDeRee") in consideration for $ 4,957 thousands (44,400 Rand) in cash and 5% of the share capital of Frutarom South Africa (Which was estimated in about $ 610 thousands).

JannDeRee, which was founded in 1993, develops, manufactures, and markets savory and sweet flavor solutions. JannDeRee has a research, development, production and marketing site in Johannesburg, South Africa, located close to Frutarom's site in South Africa, and an extensive customer base in South Africa and in other important emerging countries in the sub-Sahara region.

NOTE 5 – BUSINESS COMBINATIONS (continued):

JannDeRee's activities are synergetic with Frutarom's activities in the field of flavors South Africa.
In the twelve months ended December 31, 2012, JannDeRee's turnover amounted to approximately USD 5 million.

In the course of the third quarter of 2013 JannDeRee and Frutarom South Africa were merged into a single legal entity – Frutarom South Africa, which operates in JannDeRee site, under the same management; the R&D activities, as well as marketing, sales, production and finance were all merged into one system.

The acquisition was financed using Company's self-funds and was completed at the time of signing.

The cost of acquisition was allocated to tangible assets, intangible assets and liabilities which were acquired based on their fair value at the time of the acquisition. The intangible assets which were recognized include: product formulas amounting to 8,315 thousand Rand ($ 928 thousands), customer relations amounting to 2,631 thousand Rand ($ 294 thousands) and goodwill amounting to 37,007 thousand Rand ($ 4,131 thousands). The product formulas and customer relations are amortized over economic useful lives of 20 years and 10 years, respectively.

Set forth below are the assets and liabilities of JannDeRee at date of acquisition:

	Fair value
	U.S. dollars
	In thousands
Current assets:	
Cash and cash equivalents	139
Trade receivables	836
Inventory	336
Non-current assets:	
Property, plant and equipment	369
Intangible assets:	
Product formulas	928
Customer relations	294
Goodwill	4,172
Current liabilities:	
Trade payables	(357)
Other payables	(336)
Non-current liabilities:	
Deferred taxes	(279)
Other	(1,145)
	4,957

NOTE 5 – BUSINESS COMBINATIONS (continued):

e. Acquisition of Vantodio Holdings Limited:

On November 18, 2013 Frutarom signed, through a Swiss subsidiary, an agreement for the acquisition of 75% of the share capital of the Cypriot Vantodio Holdings Limited company ("Vantodio"), holder of the Russian Protein Technologies Ingredients group ("PTI") in consideration for a cash payment of $ 50.3 million (based on company value of $ 67 million). The acquisition was completed on November 20, 2013. The acquisition agreement offers a mutual option for Frutarom to purchase Vantodio's remaining 25% of shares starting from the end of the third year until the end of the fifth year, on the basis of a multiplier of between six and seven on the average EBITDA achieved over the three years preceding exercise and other performance factors. As of acquisition date the price of the option is $ 28,176 thousands.
Considering the fact that terms of the option are identical for all parties of the transaction, the group recorded the acquisition of full control (100%) in PTI including recording the whole liability arising from exercise of the option in the discounted value.
The results of the company were consolidated into the financial statements of the Group commencing October 1, 2013.

The acquisition was financed in full through bank credit.

PTI, established in 1996, deals in the development, manufacture and marketing of unique and innovative savory solutions including flavors, spice mixes and functional raw materials for the food industry (including specialty protein based raw materials it manufactures using advanced technology), with a special emphasis on processed meat and convenience foods.
In addition, PTI manages trade and marketing activities including, as part of the services it offers its customers in providing comprehensive solutions, providing its customers with raw materials not manufactured by PTI. This trade and marketing activities are not part of Frutarom's core activities.

PTI has two production sites near Moscow, and a modern R&D, distribution and sales center and in Moscow which includes development and application laboratories and some 25 distribution sites throughout Russia and in other countries in the region.

PTI's activities are synergetic with Frutarom's activities. The acquisition of PTI significantly strengthen Frutarom's technological capacities and the product portfolio Frutarom offers its customers throughout the world in the area of savory flavors and functional products, and will strengthen its expansive global customer base.

PTI's sales turnover in the year ended December 31, 2013 amounted to $ 115.2.

The cost of acquisition was allocated to tangible assets, intangible assets and liabilities which were acquired based on their fair value at the time of the acquisition. The intangible assets which were recognized include: product formulas amounting to 386,066 thousand Ruble ($ 11,895 thousands), customer relations amounting to 182,892 thousand Ruble ($ 5,635 thousands) and goodwill amounting to 673,323 thousand Rubles ($ 20,745 thousands). The product formulas and customer relations are amortized over economic useful lives of 20 years and 10 years, respectively.

NOTE 5 – BUSINESS COMBINATIONS (continued):

Set forth below are the assets and liabilities of PTI at date of acquisition:

	Fair value
	U.S. dollars In thousands
Current assets:	
Cash and cash equivalents	22
Accounts receivable:	
Trade	15,703
Inventory	20,715
Other	5,718
Non-current assets:	
Property, plant and equipment	10,721
Intangible assets:	
Computer software	130
Product and formulas	11,987
Customer relations	5,635
Goodwill	20,745
Current liabilities:	
Trade payables	(3,997)
Other payables	(5,356)
Non-current liabilities:	
Other	(30)
Deferred income taxes	(3,530)
Liability for put option	(28,176)
	50,287

f. Acquisition of International Aroma Group

On November 25, 2013, Frutarom signed, through a Swiss subsidiary, an agreement for purchase of the full share capital of the International Aroma Group, a Panamanian company, holder of the Guatemalan Aroma group ("Aroma"), in return for a net cash payment of $12.5 million ($13 million, net of Aroma's cash balance and cash equivalents in the amount of $0.5 million as of acquisition date). A total of $ 3 million out of the said amount has not yet been paid. This amount serves as collateral to secure to sellers liability under the purchase agreement; the said amount shall be released in installments through March 30, 2017. The share purchase agreement contains a mechanism for payment of future consideration, which was estimated by the company to a total of $ 2.3 million, under which an additional payment will be made at the rate of the EBITDA achieved in excess of $ 2.25 million over the years 2013 to 2015. The results of this company were included in the Group's consolidated financial statements as from December 1, 2013.

The transaction was financed through the Company's cash balance.
Aroma, established in 1990, deals in the development, manufacture and marketing of flavor solutions, including mainly sweet flavors for beverages, dairy products, confectionary, snack food and convenience foods.

NOTE 5 – BUSINESS COMBINATIONS (continued):

Aroma has a production, development and marketing site in Guatemala City and an extensive customer base which includes leading international food and beverage manufacturers as well as local food and beverage manufacturers in Guatemala, Honduras, Costa Rica, El Salvador and other developing countries, mainly in Central America.

In the year ended December 31, 2013, Aroma's sales turnover amounted to $ 6.2 million.

It is the Company's intention to integrate its activities in Costa Rica with Aroma's activities, which will become a center for research, development and production for countries in Central America. It is the Company's estimate that the acquisition will allow Frutarom to strengthen and deepen its presence and market sector in these developing markets in Central and South America, while expanding its product portfolio and increasing its research, development, marketing and sales infrastructure, with an emphasis on local production options and improving its customer service in the region.

The cost of acquisition was allocated to tangible assets, intangible assets and liabilities which were acquired based on their fair value at the time of the acquisition. The intangible assets which were recognized include: product formulas amounting to $ 1,312 thousand, customer relations amounting to $ 4,066 thousand and goodwill amounting to $ 6,901 thousand. The product formulas and customer relations are amortized over economic useful lives of 20 years and 10 years, respectively.

The determination of the fair value of the assets and liabilities is subject to a final appraisal of the allocation of the purchase prices to the fair value of the assets and liabilities; this appraisal, which is conducted by the Company, has not yet been completed as of the date of approval of these financial statements.

Set forth below are the assets and liabilities of Aroma at date of acquisition:

	Fair value
	U.S. dollars In thousands
Current assets:	
Cash and cash equivalents	572
Accounts receivable:	
Trade	1,282
Inventory	1,101
Other	846
Non-current assets:	
Property, plant and equipment	774
Intangible assets:	
Product formulas	1,312
Customer relations	4,066
Goodwill	6,901
Current liabilities:	
Trade payables	(304)
Other payables	(87)
Deferred income taxes	(1,120)
	15,343

NOTE 5 – BUSINESS COMBINATIONS (continued):

g. Acquisition Hagelin & Company Inc. and BRC Operating Company LLC

On December 11, 2013, Frutarom, signed an agreement, through a Frutarom subsidiary in the United States, for the acquisition of 100% of the share capital of the US based Hagelin & Company Inc. and all holdings in the US based BRC Operating Company LLC (jointly: "Hagelin"), in return for a cash payment of $52,400 thousands.

The transaction was financed through the Company's bank credit.

Hagelin, founded in 1967, develops, produces and markets flavors and unique flavor technologies for the food industry, with an emphasis on the growing area of beverage flavors. Hagelin specializes, among other things, in the development of advanced flavor technologies in the areas of sodium reduction, sugar and calorie reduction and flavor enhancement. Hagelin's customer base includes leading international food and beverage manufacturers as well as local food and beverage manufacturers in the US, the UK and in developing markets, mainly in Central and South America and in Africa.

Hagelin has three R&D, production and marketing sites, two in the United States (in New Jersey and in Georgia), and one in the UK. Hagelin's activities are to a large extent synergetic with Frutarom's activity in the US. Frutarom is acting to integrate Hagelin's activities in the UK with Frutarom's growing activity in the UK, and to integrate Hagelin's activity in Central and South America and in Africa with Frutarom's local activities in these regions.

In the year ended December 31, 2013, Hagelin's sales turnover amounted to $23.6 million.

The cost of acquisition was allocated to tangible assets, intangible assets and liabilities which were acquired based on their fair value at the time of the acquisition. The intangible assets which were recognized include: product formulas amounting to $ 6,243 thousand, customer relations amounting to $ 7,921 thousand and goodwill amounting to $ 34,114 thousand. The product formulas and customer relations are amortized over economic useful lives of 20 years and 10 years, respectively.

NOTE 5 – BUSINESS COMBINATIONS (continued):

Set forth below are the assets and liabilities of Hagelin at date of acquisition:

	Fair value
	U.S. dollars In thousands
Current assets:	
Cash and cash equivalents	288
Accounts receivable:	
Trade	2,354
Inventory	2,425
Other	467
Non-current assets:	
Property, plant and equipment	695
Intangible assets:	
Product formulas	6,243
Customer relations	7,921
Goodwill	34,114
Current liabilities:	
Trade payables	(929)
Other payables	(1,168)
Deferred income taxes	(10)
	52,400

h. Acquisition of CitraSource

On February 24, 2014 Frutarom signed, through a Frutarom subsidiary in the United States, agreements for purchase of the business activity and assets of CitraSource LLC. and 100% of the issued share capital of CitraSource Holdings LLC of Florida, USA ("CitraSource"), which includes, inter alia, a plant for processing specialty citrus ingredients, and inventory, and an agreement for the purchase of a refrigerated tank farm used by CitraSource in its routine activities. The acquisition was made in return for a net cash payment of US$7.1 million and also includes additional future payment based upon CitraSource's performance over 2014-2018, which was estimated in the amount of US$3.1 million.

The acquisition was funded using bank credit.

CitraSource, founded in 2003, specializes in research and development, production, marketing and sale of specialty solutions in the field of citrus products to leading global customers in the flavor and aroma, food and beverage markets.

CitraSource's revenues in 2013 grew to US$7 million. CitraSource's customers include leading global flavors, food and beverage manufacturers. CitraSource has extensive knowhow and excellent capabilities for the production of unique materials and flavors across all ranges of citrus (in particular oranges, lemons, grapefruits and tangerines). CitraSource also has global purchase capabilities in citrus, which will contribute to Frutarom's global purchase system.

CitraSource's activities have been integrated into the Specialty Fine Ingredients of Frutarom.

NOTE 5 – BUSINESS COMBINATIONS (continued):

The cost of acquisition was allocated to tangible assets, intangible assets and liabilities which were acquired based on their fair value at the time of the acquisition. The intangible assets which were recognized include: product formulas amounting to $ 1,379 thousand, customer relations amounting to $ 1,340 thousand and goodwill amounting to $ 2,259 thousand. The product formulas and customer relations are amortized over economic useful lives of 20 years and 10 years, respectively.

Set forth below are the assets and liabilities of CitraSource at date of acquisition:

	Fair value
	U.S. dollars In thousands
Current assets:	
Inventory	2,100
Non-current assets:	
Property, plant and equipment	3,100
Intangible assets:	
Product formulas	1,379
Customer relations	1,340
Goodwill	2,259
Non-current liabilities:	
Other payables	(3,096)
	7,082

As from the date it was consolidated with the financial statements of the Company through December 31, 2014, the acquired operations have yielded revenues of $ 8,573 thousands and net profit of $ 1,027 thousands (net of acquisition costs and finance expenses).

i. Acquisition of the flavors and natural food colors division of Montana S.A.

In October 2014 Frutarom completed the acquisition of the flavors and natural food colors division of the Peruvian company Montana S.A. ("Montana Food"). The transaction was carried out through Frutarom subsidiaries in Switzerland and the UK, and was financed entirely through the use of bank loans. No changes were made to the Company's financial covenants. The operations were consolidated into the Group's financial reports as of November 1, 2014.

The purchase was executed in exchange for payment in cash of approximately USD 24.9 million and the assumption of debts amounting to approximately USD 7.1 million. The consideration reflects a multiple of 7 times Montana Food's EBITDA for 2013.

In addition to the operations in Peru, Frutarom also acquired Montana Food's activities in Chile for no further consideration than outlined above. The purchase agreement includes a mechanism for future consideration whereby an additional payment will be made in the amount of twice the improvement in gross profit of the acquired activities over current gross profit during the 18 months following the closing of the transaction.

Montana Food is a division of Montana S.A which was founded in 1964 (which, in addition to the acquired operations, is also involved in the agricultural and feed ingredient business) and has grown into one of South America's leading companies in the field of flavors and natural food colors. Its customers include some of the world's leading global food, beverages and flavor companies as well as manufacturers based locally in South America and Central America.

NOTE 5 – BUSINESS COMBINATIONS (continued):

Its customers include some of the world's leading global food, beverages and flavor companies as well as manufacturers based locally in South America and Central America. Sales of flavors and natural colors, which constitute Montana Food's core activity, reached USD 29.5 million in 2013. Montana Food also maintains trade and marketing activity through which, as part of its service and the providing of comprehensive solutions to its customers, it markets ingredients that it doesn't produce itself. The scope of this activity, which will be combined with Frutarom's trade and marketing activity (not a core activity of the Company), reached USD 23 million in 2013.

Montana Food maintains an R&D, sales and marketing center and a modern, efficient production site in Lima, Peru with substantial capacity and the possibility for extensive further output expansion. The acquisition will also include Montana Food's activity in Chile which includes an R&D and marketing center and a staff of sales personnel for the Chilean market.

Montana Food employs about 250 people in Peru and about 30 in Chile.

Frutarom will act towards utilizing and integrating the R&D, sales and marketing infrastructure of the acquired activities with Frutarom's global R&D, sales and marketing infrastructure in order to leverage and capitalize on the abundance of cross selling opportunities generated by the acquisition, through both expanding the customer base and expanding the product portfolio.

The cost of acquisition is allocated to acquired tangible and intangible assets and to liabilities that were acquired based on their fair value at the time of purchase. The determination of the fair value of the assets and liabilities is subject to a final appraisal of the allocation of the purchase prices to the fair value of the assets and liabilities; this assessment is performed for the Company and has not yet been completed as of the date of approval of these financial statements.

Set forth below are the assets and liabilities of Montana Food at date of acquisition:

	Fair value
	U.S. dollars In thousands
Current assets:	
Cash and cash equivalents	1,613
Accounts receivable:	
Trade	11,596
Inventory	13,225
Other	1,902
Non-current assets:	
Property, plant and equipment	4,140
Intangible assets:	
Product formulas	1,968
Customer relations	1,968
Goodwill	3,936
Current liabilities:	
Trade payables	(6,632)
Other payables	(1,627)
Long term loan (including interest)	(7,122)
Deferred income taxes	(28)
	24,939

NOTE 5 – BUSINESS COMBINATIONS (continued):

As from the date it was consolidated with the financial statements of the Company through December 31, 2014, the acquired operations have yielded revenues of $ 8,616 thousands and net profit of $ 159 thousands (net of finance expenses).in addition, there were acquitions costs, net of $ 176 thousands.

j. Had the acquisitions, describe in 5.h and 5.i above, been completed on January 1, 2014, based on the unaudited information provided by owners of the acquiree based on the pre-acquisition accounting activity, the revenue of the Group for the year ended December 31, 2014 would have been $868,456 thousand, and net income for that year would have been $88,097 thousand.

assuming acquisitions performed in 2013 had been consolidated as of January 1, 2013 and that CitraSource, which was acquired during the first quarter of 2014, had been consolidated as of March 1, 2013), and that Montana food, which was acquired during the last quarter of 2014, had been consolidated as of November 1, 2013) Frutarom sales in 2013 would have reached $799,270 thousand.

The above results include interest expenses for loans to finance the acquisition that would have been registered in that period, depreciation and amortization that may have been recognized in that period for amortization of intangible assets and one-off expenses recognized on acquisition date. In the aforesaid calculation were not taken in the account of synergies that would get accepted from merger of the acquisitions with activity of the company.

NOTE 6 – SEGMENT REPORTING

a. Operating Segments

The core activity of the Group is organized to support management to perform on a worldwide basis in two major operating activities: Flavors and Fine Ingredients. Another operating activity is Trade and Marketing (each operation is considered to be a reportable segment (Note 2d). Results of operating segments are measured based on operating income.

Frutarom's Flavors Activity develops, produces, markets and sells high-quality, value added sweet and savory flavors used mainly by manufacturers of food and beverages and other consumer products including flavors and Food Systems products (products combining fruits, vegetables and/or other natural ingredients, including sweet and non-sweet flavors. These products are used in a wide variety of food products such as dairy, ice cream, sweets, salty baked products, convenience food and other prepared meals). As part of Frutarom's Specialty Fine Ingredients Activity develops, produces, markets and sells natural flavor extracts, natural functional food ingredients, natural pharma/nutraceutical extracts, natural algae based biotechnical products, aroma chemicals specialty essential oils, unique citrus products, natural gums and stabilizers. The Specialty Fine Ingredients products are sold primarily to the food and beverage, flavor and fragrance, pharmaceutical/nutraceutical, cosmetics and personal care industries.

The Trade and Marketing activity is not considered a core activity, and focuses in trade and marketing of raw materials produced by third parties, as part of providing a complete set of solutions and services to customers;

These operations are the basis on which the Group reports its primary segment information.

FRUTAROM INDUSTRIES LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 6 – SEGMENT REPORTING (continued):

Segment data provided to the chief operating decision-maker in respect of the reported segments for the year ended:

31 December, 2014 is as follows:

	Flavors operations	Fine ingredients operations	Trade and marketing operations	Eliminations	Total Consolidated
Income statement data:	U.S. dollars in thousands				
Sales – net:					
Unaffiliated customers	589,763	151,264	78,520	-	819,547
Intersegment	-	7,111	-	(7,111)	-
Total sales and other operating income	589,763	158,375	78,520	(7,111)	819,547
Segment results	97,205	19,490	2,679	(450)	118,924
Financial expenses – net					10,089
Taxes on income					21,219
Net income					87,616

31 December, 2013 is as follows:

	Flavors operations	Fine ingredients operations	Trade and marketing operations	Eliminations	Total Consolidated
Income statement data:	U.S. dollars in thousands				
Sales – net:					
Unaffiliated customers	494,389	139,597	39,707	-	673,693
Intersegment	-	5,994	-	(5,994)	-
Total sales and other operating income	494,389	145,591	39,707	(5,994)	673,693
Segment results	68,754	17,237	916	(150)	86,757
Financial expenses – net					7,528
Taxes on income					15,608
Net income					63,621

31 December, 2012 is as follows:

	Flavors operations	Fine ingredients operations	Trade and marketing operations	Eliminations	Total Consolidated
Income statement data:	U.S. dollars in thousands				
Sales – net:					
Unaffiliated customers	457,341	138,318	22,342	-	618,001
Intersegment	-	2,445	-	(2,445)	-
Total sales and other operating income	457,341	140,763	22,342	(2,445)	618,001
Segment results	59,477	12,378	1,000	(7)	72,848
Financial expenses – net					7,240
Taxes on income					13,628
Net income					51,980

NOTE 6 – SEGMENT REPORTING (continued):

b. Additional information:

1) Geographical Segment information

The Group has operating production facilities in Europe, North America and Latin America, Israel, South Africa and Asia. In addition, the Group has 42 research and development laboratories and sells and markets its products principally through its 73 sales and marketing offices.

2) Sales by Destination Based on End Customer Location
Following are data regarding the distribution of the Company's sales by:

	Year ended 31 December		
	2014	**2013**	**2012**
	U.S. dollars in thousands		
Emerging Market*	376,410	267,957	222,525
West Europe**	280,898	264,205	262,479
USA	91,590	66,799	63,906
Other	70,649	74,732	69,091
	819,547	673,693	618,001

* Sales in Russia amounted to $ 165,638 thousands, $ 89,928 thousands and $ 54,516 thousands in 2014, 2013 and 2012, respectively.

** Sales in Germany amounted to $ 72,570 thousands, $ 71,943 thousands and $ 74,085 thousands in 2014, 2013 and 2012, respectively.

NOTE 7 – PROPERTY, PLANT AND EQUIPMENT

a. Composition of assets, grouped by major classifications and changes therein in 2014 is as follows:

	Cost					Accumulated depreciation					Depreciated balance
	Balance at Beginning of year	**Additions during the year**	**Retirements during the year**	**Other***	**Balance at end of year**	**Balance at beginning of year**	**Additions during the year**	**Retirements during the year**	**Other***	**Balance at end of year**	**31 December 2014**
	U.S. dollars in thousands					**U.S. dollars in thousands**					
Land and buildings	170,324	7,894	(115)	(15,115)	162,988	49,241	3,937	(100)	(5,335)	47,743	115,245
Machinery and equipment	198,509	10,045	(1,961)	(14,795)	191,798	140,368	9,620	(1,580)	(12,670)	135,738	56,060
Vehicles and lifting Equipment	9,067	1,474	(971)	(1,356)	8,214	5,509	1,155	(734)	(910)	5,020	3,194
Furniture and office equipment (including computers)	44,419	1,072	(1,159)	(3,250)	41,082	24,665	1,555	(1,139)	(1,707)	23,374	17,708
Leasehold improvements	15,466	907	-	290	16,663	9,435	913	-	(277)	10,071	6,592
	437,785	21,392	(4,206)	(34,226)	420,745	229,218	17,180	(3,553)	(20,899)	221,946	198,799

NOTE 7 – PROPERTY, PLANT AND EQUIPMENT (continued):

a. Composition of assets, grouped by major classifications and changes therein in 2013 is as follows:

	Cost					Accumulated depreciation					Depreciated balance
	Balance at Beginning of year	**Additions during the year**	**Retirements during the year**	**Other***	**Balance at end of year**	**Balance at beginning of year**	**Additions during the year**	**Retirements during the year**	**Other***	**Balance at end of year**	**31 December 2013**
	U.S. dollars in thousands					**U.S. dollars in thousands**					
Land and buildings	152,743	7,876	(29)	9,734	170,324	43,883	4,190	-	1,168	49,241	121,083
Machinery and equipment	177,087	9,340	(859)	12,941	198,509	124,146	9,272	(894)	7,844	140,368	58,141
Vehicles and lifting Equipment	6,605	900	(1,095)	2,657	9,067	4,216	950	(980)	1,323	5,509	3,558
Furniture and office equipment (including computers)	40,696	1,340	(190)	2,573	44,419	21,541	1,563	(192)	1,753	24,665	19,754
Leasehold improvements	13,389	655	(39)	1,461	15,466	7,910	829	(32)	728	9,435	6,031
	390,520	20,111	(2,212)	29,366	437,785	201,696	16,804	(2,098)	12,816	229,218	208,567

* Arising from acquisition of consolidated companies and operations and from translation of foreign currency financial statements of consolidated subsidiaries.

NOTE 7 – PROPERTY, PLANT AND EQUIPMENT (continued):

b. Lease of land

1) Frutarom Ltd. has a leasehold right in land located in the Akko Industrial Zone and the Haifa Bay. The net capitalised lease fees as at December 31, 2014, in respect of the said lands, amount to$ 1,077 thousands (2013- $ 1,109 thousand). The leasing period is 49 years ending in the years 2032 through 2042. Frutarom Ltd. has a right to extend the leasing for an additional 49-year period.

2) A subsidiary in China has “Land Use Rights” on land in China. The rights are for a period of 50 years ending in 2046. Net capitalised lease fees as at December 31, 2013, in respect of the said land, amount to $ 159 thousand (2013 - $ 167 thousand).

3) In 2011, a subsidiary in China acquired “Land Use Rights” on land in China for the purpose of erecting a plant in China. The rights are for a period of 50 years. The cost presented in these financial statements is $ 6,900 thousands. The company expects the new plant in China to already begin operating in the second quarter of 2015.

4) In 2013, Frutarom Ltd. received a permit for allocation of land for the purpose of building a plant in the Mevo'ot Gilboa Business Park. The term of the lease rights for the land is 49 years. The cost presented in these financial statements is $ 3,776 thousands.The preliminary planning stage has been completed.

NOTE 8 – INTANGIBLE ASSETS:

	Original amount		Amortized balance	
	31 December		31 December	
	2014	2013	2014	2013
Know-how and product formulas	72,699	77,846	52,285	59,853
Goodwill	247,203	273,749	245,968	272,475
Customer relations	61,959	65,175	35,777	43,121
Trademarks	576	408	218	172
Computer software	25,106	26,839	5,562	8,108
	407,543	444,017	339,810	383,729

NOTE 8 – INTANGIBLE ASSETS (continued):

Composition of Intangible Assets, Grouped by Major Classifications and Changes Therein is as Follows:

	Computer software	**Know-how and Product formulas**	**Goodwill***	**Customer relations**	**Trademarks**	**Total**
			U.S. dollars in thousands			
Balance as of 1 January 2013 – net	10,017	41,782	197,493	29,807	99	279,198
Changes in the year ended 31 December 2013:						
Acquisitions	695	173	-	-	-	868
Retirements during the year	-	-	-	-	-	-
Adjustment arising from acquisition of consolidated companies	130	20,380	71,892	17,916	92	110,410
Exchange differences	279	423	3,090	349	1	4,142
Annual amortization charge (Note 2f)	(3,013)	(2,905)	-	(4,951)	(20)	(10,889)
Closing net book amount	8,108	59,853	272,475	43,121	172	383,729
Changes in the year ended 31 December 2014:						
Acquisitions	958	-	-	-	114	1,072
Retirements during the year	-	(15)	-	-	-	(15)
Adjustment arising from acquisition of consolidated companies	-	4,038	5,503	3,308	-	12,849
Exchange differences	(721)	(7,703)	(26,190)	(3,995)	(25)	(38,634)
Changes in the excess of cost of acquisition	-	-	(5,820)	-	-	(5,820)
Annual amortization charge (Note 2f)	(2,783)	(3,888)	-	(6,657)	(43)	(13,371)
Closing net book amount	5,562	52,285	245,968	35,777	218	339,810

* Goodwill as of 31 December 2014 is allocated to the Flavor segment in the U.K., Germany, Israel, Norway, Italy, USA, Brazil, South Africa, Russia , Guatemala & Peru and to the Fine Ingredients segment in Belgium, USA and the UK.

NOTE 8 – INTANGIBLE ASSETS (continued):

Impairment test for goodwill

The goodwill recorded in the Group's books of accounts arises from acquisitions of consolidated companies and operations carried out by the Group over the years, the goodwill is allocated to the cash-generating units of the Group in accordance with the unit and the business segment from which it arises.

Set forth below is a summary of goodwill allocation between the various cash-generating units:

	31 December	
	2014	2013
	U.S. dollars in thousands	
Cash-generating unit 1	95,499	108,247
Cash-generating unit 2	70,234	76,194
Cash-generating unit 3	15,324	16,257
Cash-generating unit 4	11,285	20,536
Cash-generating unit 5	10,659	11,306
Cash-generating unit 6	7,511	8,454
Cash-generating unit 7	7,041	6,901
Cash-generating unit 8	6,180	7,008
Cash-generating unit 9	5,848	6,205
Cash-generating unit 10	4,266	2,699
Cash-generating unit 11	3,770	-
Cash-generating unit 12	3,234	3,549
Cash-generating unit 13	2,619	2,619
Cash-generating unit 14	2,498	2,498
Total	245,968	272,475

The changes in goodwill between the years are due to acquisitions of new companies/operations, changes in the exchange rate of the currency of the foreign operation compared with the dollar as explained in Note 5.

The recoverable amount of a cash-generating unit is determined based on value-in-use calculations. These calculations use pre-tax cash flow projections based on past results of the unit, its budget for the following year and the projection for future years, cash flows from the fifth-year are extrapolated using a grow rate of 2.5%-3%, according to the activity area of the cash generating unit, which does not exceed the long-term growth rate for the food business and the relevant areas, in which the Group operates.

The average discount rate taken into account in the calculation is 14.7% before taxes.

Group management determined profit rates based on past performance and its expectations for developments in respect of each of the cash-generating units.

The recoverable amount of cash-generating unit 1 and 2 was calculated and examined by an external assessor, whereas the recoverable amount of the remaining cash-generating units was calculated and examined by Group management.

The results of the above analysis show that the value of goodwill of each of the said cash-generating units has not been impaired, both in the basic calculations and in calculations performed for the purpose of sensitivity test.

NOTE 9 – BORROWINGS

	December 31	
	2014	**2013**
	U.S. dollars in thousands	
Non current borrowings	163,696	140,113
Current borrowings:		
Current maturities of long-term loans	33,581	36,678
Bank borrowings	34,169	71,548
	67,750	108,226
Total borrowings	231,446	248,339

Bank borrowings as of December 31, 2014 mature until 2018 and bears average interest of 1.39% according to the loan terms and Libor rates as of 31 December, 2014.
The exposure of the Group's cash flows to interest rate changes is dependent at the rate of Libor-Euro, Libor-Dollar, Libor-Swiss franc and Libor-Pound Sterling and it is updated on a quarterly basis.

Due to the above, the fair value of current and non-current borrowings equals their carrying amount, as the impact of discounting is not significant. The fair values are based on cash flows discounted the borrowings' discount rate.

The carrying amounts of the Group's borrowings are denominated in the following currencies:

	Weighted average interest rates*	**31 December**	
		2014	**2013**
		U.S. dollars in thousands	
Pound sterling	1.50%	27	13,853
Dollars	1.57%	105,868	151,679
Euro	1.35%	21,356	34,705
Swiss Franc	1.29%	103,302	46,127
Other currencies	7.5%	893	1,975
		231,446	248,339

* Interest rates as of 31 December, 2014

The long term liabilities (net of current maturities) mature in the following years after the balance
sheet dates:

	2014	**2013**
	U.S. dollars in thousands	
Second year	56,908	62,047
Third year	62,819	74,735
Fourth year	43,969	3,331
	163,696	140,113

The Group has several loans, in respect of which it has undertaken to meet certain financial covenants (see note 14). As of 31 December 2014 , the Group meets all the required financial covenants.

NOTE 10 – LIABILITY FOR EMPLOYEE RIGHTS UPON RETIREMENT:

a. Labour laws and agreements in Israel and abroad require the Company and part of its consolidated companies to pay severance pay and/or pensions to employees dismissed or retiring from their employ in certain other circumstances. Group companies' liability is covered mainly by regular contributions in defined contribution plans. The amounts funded as above are not reflected in the balance sheets since they are not under the control and management of the companies.

b. Under the agreement with its employees, the U.S. subsidiary financed a defined benefit plan. As part of the collective agreement signed between the Company's subsidiary and the industrial labour union on 13 October, 2000, the U.S. subsidiary suspended the said plan and joined, as from that date, a comprehensive pension plan of the labour union, which is a defined contribution plan.
The U.S. subsidiary will continue financing its existing liabilities under the suspended pension plan. The amount of liability for employee rights upon retirement and amounts funded, as presented in the consolidated accounts, reflect, inter alia, the U.S. subsidiary's liability in respect of the suspended plan.

c. The Swiss and German subsidiaries have a liability for payment of pension to employees in Switzerland and Germany under a defined benefit plan. The said liabilities have been transferred to these subsidiaries as part of the acquisition of subsidiaries in 2003 and 2007, respectively. The consolidated companies make deposits with pension plans in respect of these liabilities. The amount of the liability for pension (net) included in the balance sheet reflects the difference between the liability for pension payments and the assets of the pension fund, as detailed in d. below.

d. The Company's severance pay liability in respect of Israeli employees for whom the said liability is covered under section 14 of the Severance Pay Law is covered by regular deposits with defined contribution plans. The amounts funded as above are not reflected in the consolidated statements of financial position.

e. Amounts charged to income statement in respect of defined benefit plan in 2014, 2013 and 2012 are $ 2,250 thousands, $ 2,622 thousands and $ 986 thousands, respectively.

FRUTAROM INDUSTRIES LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 10 – LIABILITY FOR EMPLOYEE RIGHTS UPON RETIREMENT (continued):

Changes in net liability (asset):

	Present value of obligation	**Fair value of plan assets**	**Net liability (asset)**
	US dollars in thousands		
Balance as of January 1, 2014	56,872	(33,746)	23,126
Current service cost	1,747	-	1,747
Interest expenses (income)	1,338	(741)	597
Other	(94)	-	(94)
	2,991	(741)	2,250
Remeasurements of the net liability (asset):			
Return on plan assets, excluding amounts included in interest expense (income)	-	(227)	(227)
Loss (gain) from change in demographic Assumptions	-	-	-
Loss (gain) from change in financial assumptions	11,144	-	11,144
Experience loss (gain)	(310)	-	(310)
	10,834	(227)	10,607
Differences from translation of financial statements	(6,493)	3,184	(3,309)
Employer's contributions	938	(2,336)	(1,398)
Benefit payments	(2,971)	2,686	(285)
Balance as of December 31, 2014	62,171	(31,180)	30,991
Balance as of January 1, 2013	57,644	(33,315)	24,329
Current service cost	2,100	-	2,100
Interest expenses (income)	1,245	(650)	595
Other	(73)	-	(73)
	3,272	(650)	2,622
Remeasurements of the net liability (asset):			
Return on plan assets, excluding amounts included in interest expense (income)	-	172	172
Loss (gain) from change in demographic Assumptions	(422)	-	(422)
Loss (gain) from change in financial assumptions	(2,365)	-	(2,365)
Experience loss (gain)	(286)	-	(286)
	(3,073)	172	(2,901)
Differences from translation of financial statements	1,654	(870)	784
Employer's contributions	949	(2,232)	(1,283)
Benefit payments	(3,574)	3,149	(425)
Balance as of December 31, 2013	56,872	(33,746)	23,126

NOTE 10 – LIABILITY FOR EMPLOYEE RIGHTS UPON RETIREMENT (continued):

The following amounts were recognized in the statement of financial position for post-employment defined benefit plans:

	December 31	
	2014	**2013**
	U.S. dollars in thousands	
Present value of obligations arising from fully or partially funded plans	62,171	56,872
Fair value of plan assets	(31,180)	(33,746)
Balance of liability recognized in the statement of financial position	30,991	23,126

Amounts recognized in the statement of financial position for post-employment defined benefit plans are predominantly non-current and are reported as non-current liabilities.

The Group operates defined benefit schemes in several countries for which the actuarial assumptions vary based on local economic and social conditions. The assumptions used in the actuarial valuations of the defined benefit plans, were as follows:

	U.S.A.			**Germany**			**Switzerland**		
	2014	**2013**	**2012**	**2014**	**2013**	**2012**	**2014**	**2013**	**2012**
Discount rates	3.55%	3.55%	4.15%	2.28%	3.36%	3.03%	1.0%	2.0%	1.8%
Projected rates of payroll raise				1.17%	1.17%	1.16%	1.5%	2.0%	2.0%

The sensitivity of the defined benefit obligation to changes in the weighted principal assumptions assuming all other assumptions remained unchanged and which were reasonably possible and the end of the reported period is:

	Increase (decrease) in defined benefit obligation
	December 31, 2014
	US dollars in thousands
Discount rate:	
1% increase	(9,706)
1% decrease	12,772
Salary growth rate:	
1% increase	1,230
1% decrease	(1,122)

The change in the rate of retiring employees at the end of the reported period did not have a material effect on the defined benefit liability.

NOTE 10 – LIABILITY FOR EMPLOYEE RIGHTS UPON RETIREMENT (continued):

Plan assets

The plan assets are composed as follows:

	2014	2013
	US dollars in thousands	
Government bonds	2,691	2,547
Real estate held abroad	3,121	3,421
Qualifying insurance policies	1,030	1,004
Cash and cash equivalents	21,619	23,794
other	2,719	2,980
Total	31,180	33,746

NOTE 11 – COMMITMENTS AND CONTINGENT LIABILITIES

a. **Commitments**:

1) Lease Commitments:

Some of the Group's premises, warehouses, sites and vehicles in the U.K., Germany, Belgium and Israel occupied by the Group are rented under various operating lease agreements. The lease agreements for the premises will expire on various dates between 2015 and 2020.

Minimum lease commitments of the Group under the above leases, at rates in effect on 31 December 2014, are as follows:

	$ in thousands
Year ending 31 December:	
2015	5,795
2016	3,600
2017	2,835
2018	938
2019	601
2020	350
	14,119

Rental expenses totaled $ 8,027 thousand, $ 6,518 thousand and $ 5,818 thousand, in the years ended 31 December 2014, 2013 and 2012, respectively.

NOTE 11 – COMMITMENTS AND CONTINGENT LIABILITIES (continued):

2) Royalty Commitments:

Frutarom Ltd. is committed to pay royalties to the Government of Israel on proceeds from sales of products in the research and development of which the Government participates by way of grants. Under the terms of Company's funding from the Israeli Government, royalties of 3%-5% are payable on sales of products developed from a project so funded, up to 100% of the amount of the grant received by the Frutarom Ltd. (dollar linked); as from 1 January, 1999 – with the addition of an annual interest rate based on Libor.
The maximum royalty amount payable by Frutarom Ltd. at 31 December 2014 is $1,867 thousand.
In 2014, Frutarom Ltd. was of the opinion that it is more likely than not that it would not be required to refund Chief Scientist grants in the total amount $53 thousand (2013 - $31 thousand); therefore it carried this amount to income.

b. Contingent Liabilities:

The consolidated companies of the Group are not a party to legal procedures in the ordinary course of business, which in the opinion of Group's management are materially affect the Group's financial position.

NOTE 12 – EQUITY:

a. Share Capital:

1) Composed of ordinary shares of NIS 1 par value, as follows:

	Number of shares in thousands and the amount thereof, denominated in NIS	
	December 31	
	2014	2013
Authorized	100,000	100,000
Issued and paid	58,661	58,509

Company listed shares are quoted on the TASE at NIS 120.5 ($30.98) per share as of 31 December, 2014. The GDRs representing the Company's shares are quoted on the official list of the LSE.

2) Ordinary Company shares of NIS 1 par value, are held by the company and included in the issued and paid share capital constitute 0.5% (314,890 shares) and 0.6% (323,183 shares) of the balance of ordinary issued and paid shares of this type as of 31 December 2014 and 2013, respectively.
The purchase cost of those shares was deducted from equity as part of "Cost of Company's shares held by the company" balance. The shares are held as "Treasury Shares".

NOTE 12 – EQUITY (continued):

b. Employee Shares and Option Plans for Senior Employees of Subsidiaries:

1) Commencing 2003 and on a semi-annual basis, the Board of Directors resolves to allot options to senior managers and other senior employees based on the recommendations of the remuneration committee. In accordance with the Board of Directors' resolution and taking into consideration the number of shares available to the Company for the purpose of allotment of the options, the Company acquires Company shares in the Stock Exchange and grants the options against those shares.

Until the first half of 2011 the options were granted in accordance with the 2003 option plan. Commencing 2012, the options are granted in accordance with the 2012 option plan ("the 2012 plan"). The options are exercisable in three equal batches at the end of every year for a period of 3 years from date of grant. The Board of Directors has the exclusive right to declare the exercise of the options at an earlier date, and with regards to senior office holders – in accordance with compensation policy, in extraordinary cases and under weighty considerations.
The exercise price of the option granted in accordance with the said plans, as set determined by the Board of Directors equals a third of the average purchase price paid by the Company in respect of those shares. Options granted under this plan expire at the end of 6 years from date of grant. All tax liabilities arising from grant of options and/or from exercise thereof apply to the employee. The number of exercised shares in respect of each option, as well as the exercise price are adjusted in accordance with the changes in the Company's share capital, such changes originating in split of shares, consolidation of shares, dividend distributed in shares and/or creation of new types of shares, excluding a number of exceptions where the employer-employee relationship between the Company and an employee are terminated; in such a case the employee shall be entitled to exercise all the options exercisable at the date of termination of employer-employee relationship within 90 days from the said date. The remaining options granted to the employee and which were not exercised by the employee shall expire.

Options that are not exercisable at the time of termination of the employer-employee relationship shall expire immediately upon termination of the relationship as above.

Commencing 2013 the grant of options in accordance with plan 2012 to the Company's president and CEO ("CEO") is included in the equity component of the annual bonus; (for details regarding the compensation policy of the CEO, see Company's report of June 29, 2013 (reference 2013-01-076263)). Commencing 2014 and based on the Company's compensation policy which was approved on January 14, 2014, the grant of options in accordance with plan 2012 to all senior office holders including the Company's president and CEO is included in the equity component of the annual bonus; (for details regarding the compensation policy which was approved, see Company's report of December 29, 2013 (reference 2013-01-111694)).

NOTE 12 – EQUITY (continued):

The theoretical economic value of the options in respect of grants from 2007 through 2014, is based on the following assumptions: expected dividend yield of 0% for each one of the years 2007-2011, beginning from 2012 dividend yield expected of 0.44%, expected volatility of 17.74%-24.32%; risk-free interest rate of 2.2%-3.98% (based on the expected term of the option until exercise); and expected term until exercise of: two years in respect of the first batch, three years in respect of the second batch and four years in respect of the third batch.

The 2012 plan is managed in compliance with the provisions in section 102 to the Israel Income Tax Ordinance.

In accordance with the track chosen by the company and pursuant to the terms thereof, the company is allowed to claim, as an expense for tax purposes, the work income component credited to employees, and is not entitled to claim as an expense for tax purposes the amounts credited to employees as equity benefits.

2) Set forth below are data regarding the options under the 2003 & 2012 Plans, which have not yet been exercised by Company employees, as of December 31, 2014:

Year of grant	**Number of options in respect of which the vesting period ended**	**Number of options in respect of which the vesting period has not yet ended**	**Exercise price $**
2009	1,659	-	2.66
2010	10,139	-	3.02-3.09
2011	9,340	-	3.11
2012	96,332	45,154	2.84-3.12
2013	29,537	63,376	4.27-5.17
2014	-	58,803	7.37-7.74
	147,007	314,340	

As of 31 December, 2014, the remaining amount of compensation, computed as the excess or the fair value of the said options granted to employees over the exercise price at the date of grant not yet recorded as expenses in the income statements is approximately $847 thousand. The said remaining compensation will be charged to income using the accelerated method over the remaining vesting period.

As to options granted to the president of the Company - Note 21.a.2.

NOTE 12 – EQUITY (continued):

The changes in the number of options outstanding and their related weighted average exercise prices are as follows:

	2014		2013		2012	
	Average exercise price in U.S. $ Per share	Options	Average exercise price in U.S. $ per share	Options	Average exercise price in U.S. $ per share	Options
Outstanding at 1 January	3.99	317,801	3.10	462,036	2.97	417,342
Granted	7.55	59,698	5.25	103,192	3.15	228,914
Forfeited	4.41	(9,905)	3.26	(37,778)	3.08	(32,111)
Exercised	3.35	(53,254)	2.98	(209,649)	2.78	(152,109)
Balance at 31 December	4.37	314,340	3.99	317,801	2.97	462,036

The following table summarizes information about exercise price and the contractual terms of options outstanding at 31 December, 2014:

Share rights outstanding			Share rights exercisable		
Exercise Prices	Number outstanding at December 31, 2014	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable at December 31, 2014	Weighted average remaining contractual life
$		Years	$		Years
2.66	1,659	0.75	2.66	1,659	0.75
3.09	2,104	1.25	3.09	2,104	1.25
3.02	8,035	1.75	3.02	8,035	1.75
3.11	9,340	2.25	3.11	9,340	2.25
2.84	29,928	2.75	2.84	29,928	2.75
3.12	44,058	3.25	3.12	25,067	3.25
3.08	67,500	3.75	3.08	41,337	3.75
4.27	50,258	4.25	4.27	15,913	4.25
5.17	42,655	4.75	5.17	13,624	4.75
7.37	29,422	5.25	7.37	-	5.25
7.74	29,381	5.75	7.74	-	5.75
	314,340			147,007	

3) On 15 July 2010 the Company's Board of Directors approved a plan to grant options to senior managers ("the 2010 plan").
The options granted under this plan are exercisable in three equal batches at the end of each year commencing the end of the second year from date of grant thereof. The Board of Directors has the exclusive authority to declare the exercise of the options at an earlier date. Options granted under these plans expire within six years from date of grant. All tax liabilities arising from grant of options and/or from exercise thereof apply to the employee.

NOTE 12 – EQUITY (continued):

The number of exercised shares in respect of each option, as well as the exercise price are adjusted in accordance with the changes in the Company's share capital, such changes originating in split of shares, consolidation of shares, dividend distributed in shares and/or creation of new types of shares, excluding a number of exceptions where the employer-employee relationship between the Company and an employee are terminated; in such a case the employee shall be entitled to exercise all the options exercisable at the date of termination of employer-employee relationship within 90 days from the said date. The remaining options granted to the employee and which were not exercised by the employee shall expire. Options that are not exercisable at the time of termination of the employer-employee relationship shall expire immediately upon termination of the relationship as above.

At the date of approval of the 2010 plan, based on the recommendations of the remuneration committee, the Board of Director approved the grant of up to 1,000,000 options (not registered for trade) to the company president and 10 further employees and office holders in the Group; the Board also approved the grant of additional 255,000 options to employees and office holders in the Group ("options for future allocation"). The grant of options to the company president was also approved by the Company's Audit Committee. The options were granted without consideration.

As part of the this grant, the exercise price of the options was NIS 30.26 which is the closing price of Company's share on the last trading day prior to Board's resolution on such allocation. Each option for future allocation that will be granted to future offerees as part of this grant will be exercisable into one share for an exercise price that will equal an average of closing prices in the ten consecutive trading days prior a Board's resolution on such future allocation, so long as the exercise price of each future allocation option is no less than the par value of Company shares.

The fair value of the options at date of grant - computed based on the binomial model – is NIS 3.4 million ($ 0.9 million); this value is based on the following assumptions: adjusted standard deviation of 38% per year, risk-free interest rate of 3.5% and termination rate (prior to end of the vesting period) of 17%; this rate is based on a sample of the changes in manpower of offerees rank for the last several years prior to the grant.

On February 6, 2011, the Company granted 40,000 further options to a senior office holder in the Company out of the number of options designed for future allotment; (this grant was also approved by the Company's audit committee). The exercise price in respect of this grant was set to NIS 36.93 ($10.41); the exercise price is unlinked and is equal to the average closing rates of the Company's share in the 10 trading days that preceded the resolution of the Company's board as to allotment of the options. The theoretical economic value of the options at date of grant - computed using the binomial model – is NIS 0.2 million ($0.06 million). The rest of options designed for future allotment expired in the date of the publication of company financial reports for 2010.

NOTE 12 – EQUITY (continued):

On August 20, 2012, the Company's Board of Directors approved the grant of up to 945,000 options (not registered for trade) as part of the 2010 plan to the president and 10 other employees and office holders in the Group; the Board also approved the future grant of up to 200,000 further options to employees and office holders in the Group ("the future options"); the resolution was made based on the recommendations of the remuneration committee. The grant of options to the senior office holders was also approved by the Company's Audit Committee. The options were granted without consideration.

Each option is exercisable into one share for an exercise price of NIS 34.85 which is the closing price of Company's share on the last trading day prior to Board's resolution on such allocation. Each future option that will be allotted to future offerees as part of this grant will be exercisable into one share for an exercise price that will equal an average of closing prices in the ten consecutive trading days prior a Board's resolution on such future allocation, so long as the exercise price of each future allocation option is no less than the par value of Company shares. On 1 October, 2012, the Company's Board of Directors approved the allotment of 120,000 options to another senior office holder in the Company as part of this grant plan.this grant was also approved by the Company's Board of Directors. The exercise price in respect of this grant was set to NIS 37.75. The options granted during this grant expired before vesting following the termination of employment of senior office holder in the company. The remaining of options designed for future allotment expired on the date of the publication of the company's annual financial statements for 2012.

On August 19, 2014, the Company's Board of Directors approved the grant of up to 522,500 options (not registered for trade) as part of the 2010 plan to the president and 10 other employees and office holders in the Group; the Board also approved the future grant of up to 150,000 further options to employees and office holders in the Group ("2014 future options"); The options were granted without consideration.
The allocation of options to all senior office holders, including the President & CEO, is in accordance with the Company's compensation policy**.**
Each option is exercisable into one share for an exercise price of NIS 89.21 which is the average closing price of Company's share over the 30 trading days prior to Board's resolution on such allocation, plus 5%. As of the date of publication of this report, the futures options of 2014 expired without haven been granted to any offerees.
The fair value of the options at date of grant **-** computed based on the binomial model – is NIS 4.9 million ($ 1.4 million); this value is based on the following assumptions: adjusted standard deviation of 23.34% per year, risk-free interest rate of 0.33% and termination rate (prior to end of the vesting period) of 11.1%; this rate is based on a sample of the changes in manpower of offerees rank for the last several years prior to the grant.

As to the fair value of the options granted to the president – see note 21.a.2.

The 2010 plan is managed in compliance with the provisions in section 102 to the Israel Income Tax Ordinance.

The Group creates deferred taxes for grants that fall into the scope of IFRS 2 – "Share Based Payment" – in accordance with the proportionate part of the estimated amount deductible for tax purposes by the Group at date of exercise of benefit by the employee and in respect of which work services were provided by the employee.

NOTE 12 – EQUITY (continued):

through the date of the statement of financial position (i.e., the estimated overall amount deductible for tax purposes divided by the overall vesting period and multiplied by the vesting period that has elapsed through the date of the statement of financial position). The said deferred taxes are recognized in the statement of income.

c. Dividend and Retained Earnings

1) The amounts of the dividend paid presented in the statement of changes in shareholders' equity are net the share of the group companies holding Company shares (Note 2m). The group companies' share in the dividend is \$ 28 thousand, \$ 30 thousands and \$27 thousand in 2014, 2013, 2012, respectively.

   In determining the amount of retained earnings available for distribution as a dividend, the Companies Law stipulates that the cost of the Company's shares acquired by the group companies (that are presented as a separate item on the statement of changes in shareholders' equity) is to be deducted from the amount of retained earnings presented among Company's shareholders' equity.

2) In its meeting on March 15, 2015, the Company's Board of Directors resolved to distribute a final cash dividend out of retained earnings as of December 31, 2014; the amount of this dividend is \$5,552 thousand (NIS 22,291 thousand). Frutarom Ltd. does not intend to distribute dividend out of tax exempt income arising from "approved enterprise", as explained in Note 13c.

3) The dividend paid in 2014 and 2013 amounted to \$ 4,712 thousand (NIS 0.28 per share) and \$ 3,892 thousands (NIS 0.24 per share). As mentioned in 2) above, the dividend in respect of the year ended 31 December 2014 at NIS 0.38 per share and totaling \$5,552 thousand was discussed in the Company's Board of Directors.

NOTE 13 - TAXES ON INCOME:

a. Corporate taxation in Israel

1) Commencing 2008, the results for tax purposes of the Company and its Israeli subsidiaries are measured in nominal values. The Israeli companies are companies of foreign investors and have elected to keep their books and records in dollars for tax purposes, as permitted under the Income Tax Regulations (Principles for the Bookkeeping of Foreign Invested Companies and of Certain Partnerships and the Determination of Their Taxable Income), 1986.

2) **Tax rates**

   The income of the Company and its Israeli subsidiaries (other than income from "approved" or "beneficiary enterprises") is taxed at the regular rate; under the provisions of the Law for Amendment of the Income Tax Ordinance, 2005, of August 2005 and the provisions of the Economic Rationalization Law (Legislation Amendments for the Implementation of the Economic Plan for the years 2009 and 2010), of July 2009, the corporate tax rates is to be gradually reduced as from 2011 and thereafter, as follows: 2010 - 2011 – 24%, 2012 – 23%, 2013 – 22%, 2014 – 21%, 2015 – 20%, 2016 and thereafter – 18%.

NOTE 13 - TAXES ON INCOME (continued):

On August 5, 2013, the Law for Change of National Priorities (Legislative Amendments for Achieving the Budgetary Goals for 2013-2014), 2013 (hereinafter - the Law) was published in the official gazette, which enacts, among other things the increase of the corporate tax rate to 26.5% beginning in 2014 and thereafter. (as to the increase of tax rates applicable to income from preferred enterprise as set out in the law for the Encouragement of Capital Investment, 1959, see c below).

Capital gains of the Company are subject to tax at the regular corporate tax rate applicable during the tax year.

b. Subsidiaries outside Israel

Subsidiaries that are incorporated outside of Israel are assessed for tax under the tax laws in their countries of residence. The principal tax rates applicable to subsidiaries outside Israel are as follows:

Companies incorporated in the USA – tax rate of 41% - 42%
Companies incorporated in Germany– tax rate of 30%
Company incorporated in Belgium – tax rate of 34%
Company incorporated in Italy – tax rate of 31.4%
Company incorporated in Norway – tax rate of 27%.
Companies incorporated in the UK – tax rate of 21% (April 2013 through March 2014 tax rate of 23%; commencing April 2014 - tax rate of 21%).
Company incorporated in the Switzerland – tax rate of 22%.
Company incorporated in Slovenia – tax rate of 17%
Companies incorporated in China – tax rate of 25%
Companies incorporated in Brazil – tax rate of 34%
Company incorporated in South Africa – tax rate of 28%
Companies incorporated in Russia – tax rate of 20%
Companies incorporated in Guatemala – tax rate of 28%
Company incorporated in the Peru – tax rate of 30%.
Company incorporated in the Chile – tax rate of 21%.

c. Encouragement Laws in Israel

1) Tax benefits under the Israeli Law for the Encouragement of Capital Investments, 1959 (hereinafter - the Law)

Under the law, including Amendment No. 60 to the law that was published in April 2005, by virtue of the "approved enterprise" or "benefited enterprise" status granted to certain enterprises of the Company, and by virtue of the "Foreign Investors' Company" status it was granted, Frutarom Ltd. is entitled to various tax benefits.

2) Amendment to the Israel Capital Investment Encouragement Law, 1959

The Israel Law of Economic Policy for the Years 2011 and 2012 (Legislation Amendments), which was passed by the Knesset (the Israeli parliament) on December 29, 2010, includes an amendment to the Israel Capital Investment Encouragement Law, 1959 (hereinafter - the amendment). The amendment became effective on January 1, 2011.

NOTE 13 –TAXES ON INCOME (continued):

The amendment sets out benefit tracks to replace those provided by the Law for Encouragement of Capital Investments, 1959 (hereafter – the law) before it was amended. Key changes in programs include a grants program for entities in development area A, and two new tax benefit programs ('preferred enterprise' and 'special preferred enterprise'). In essence, these provide a uniform tax rate on the entire preferred income of an entity, as the term preferred income is defined in the amendment.

Frutarom Ltd. elected to apply the amended law commencing 2011 and to apply the tax benefits available under the "preferred enterprise" track. Accordingly, commencing 2011, the following reduced tax rates shall be applicable to the preferred income of the companies, whose plants are located in development area A/an "other" development area: 2011 and 2012 – 10%/15%; 2013-2014 – 12.5%/7% and 2015 and thereafter – 12%/6%.

The Law for Change of National Priorities (Legislative Amendments for Achieving the Budgetary Goals for 2013-2014), 2013, which was published in the official gazette on August 5, 2013, enacts among other things, the increase of the tax rate applicable to preferred income to the effect that commencing 2014 and thereafter the tax rate on the preferred income of companies whose plants are located in development area A/an "other development area" shall be 9%/16%.

Through the 2010 tax year, the Company benefited from tax breaks under the Law for Encouragement of Capital Investments prior to its amendment, which provided reduced tax rates/tax exemptions on income attributed to "approved enterprises" or "benefited enterprises" they own.
In case of distribution of cash dividend out of income that was previously tax exempt as above, the Company would have to pay the tax in respect of the amount distributed, in accordance with the tax rate that would have been applicable to the income in the year it was accumulated, had the exemption not been granted.

3) The Law for the Encouragement of Industry (Taxation), 1969:

a. Frutarom Ltd. is an “industrial company” as defined by this law. As such, Frutarom Ltd. is entitled to claim amortization over 8 years of acquired product formulas, as well as depreciation at increased rates for equipment used in industrial activity as stipulated by regulations published under the inflationary adjustments law, and have done so.

b. The Company and Frutarom Ltd. file a consolidated tax return in accordance with the Law for the Encouragement of Industry. Accordingly, each company is entitled to set-off its tax losses (created commencing the year in which consolidated reporting for tax purposes began) against the taxable income of the other company, subject to certain restrictions.

NOTE 13 –TAXES ON INCOME (continued):

d. Deferred Income Taxes

1) Composition of deferred taxes as of dates of statements of financial position and changes therein in those years are as follows:

	Depreciable fixed assets	Provisions for employee rights: Severance Pay	Provisions for employee rights: Vacation and recreation pay	Inventories	Other	Depreciable intangibles	In respect of Carry forward tax losses	Total
	U.S. dollars in thousands							
Balance at 1 January, 2013	16,595	(4,030)	(190)	(1,213)	(605)	16,467	(5,679)	21,345
Changes in 2013:								
Additional taxes as a result of acquisition of Subsidiaries	989	-	-	(749)	(515)	11,173	-	10,898
Differences from translation of foreign currency financial statements of subsidiaries	360	(133)	-	45	40	408	(245)	475
Charged directly to the equity	-	748	-	-	-	-	-	748
Amounts carried to income statement	(1,199)	(25)	(61)	(571)	(767)	277	(460)	(2,806)
Balance at 31 December 2013	16,745	(3,440)	(251)	(2,488)	(1,847)	28,325	(6,384)	30,660
Changes in 2014:								
Additional taxes as a result of acquisition of Subsidiaries	-	-	-	-	28	-	-	28
Changes in the excess of cost of acquisition	-	-	-	-	-	(5,960)	-	(5,960)
Differences from translation of foreign currency financial statements of subsidiaries	(1,555)	586	-	281	(504)	(2,865)	788	(3,269)
Charged directly to the equity	-	(2,452)	-	-	-	-	-	(2,452)
Amounts carried to income statement	(300)	(685)	16	(446)	1,512	863	533	1,493
Balance at 31 December 2014	14,890	(5,991)	(235)	(2,653)	(811)	20,363	(5,063)	20,500

NOTE 13 –TAXES ON INCOME (continued):

2) Deferred taxes are presented in the statements of financial position as follows:

	December 31	
	2014	**2013**
	U.S. dollars in thousands	
Among non-current assets	3,042	3,424
Among non-current liabilities	(23,542)	(34,084)
	(20,500)	(30,660)

3) The deferred taxes in respect of Group activities in Israel are computed at the tax rate of 16%. This rate is an average taking into account the tax rates applicable to income from Frutarom Ltd.'s preferred enterprises (in accordance with the amendment to the law, see also note 13c2).

Deferred taxes of foreign subsidiaries not in Israel are computed at the tax rates applicable to these companies (see b above).

e. Taxes on Income Included in The Income Statements for the presented periods:

1) As follows:

	2014	**2013**	**2012**
	U.S. dollars in thousands		
Current taxes:			
For the reported year's income	19,298	19,056	15,335
Adjustments in respect of previous years	428	(642)	(717)
	19,726	18,414	14,618
Deferred taxes:			
Creation and reversal of deferred taxes	1,493	(2,806)	(990)
T o t a l	21,219	15,608	13,628

Current taxes are computed in accordance with the statutory tax rates of Group entities around the world (see above) and in accordance with relevant tax benefits for each country.

NOTE 13 –TAXES ON INCOME (continued):

2) Following is a reconciliation of the theoretical tax expense, assuming all income is taxed at the regular tax rates applicable to companies in Israel (Note 13c above) and the actual tax expense:

	2014	**2013**	**2012**
	U.S. dollars in thousands		
Income before taxes on income, as reported in the income statements	108,835	79,229	65,608
Theoretical tax expense in respect of this income – at 26.5% (2013 – 25%; 2012 – 25%)	28,841	19,807	16,402
Less – tax benefit arising from approved enterprise /benefited enterprise status	(1,859)	(2,097)	(1,158)
Increase in taxes resulting from different tax rates applicable to foreign subsidiaries	(3,234)	(391)	52
Decrease in taxes arising from computation of deferred taxes at a rate which is different from the theoretical rate	(13)	(209)	(159)
Increase (decrease) in deferred taxes as a result of future changes in the tax rates	(650)	(2,089)	-
Increase (decrease) in taxes arising from permanent differences – disallowable expenses (income)	(1,231)	501	(412)
Decrease in taxes resulting from utilization, in the reported year, of carry forward tax losses and other expenses for which deferred taxes were not created (net of increase in taxes in respect of tax losses incurred in the reported year for which deferred taxes were not created)	(262)	(482)	(372)
Difference between the basis of measurement of income reported for tax purposes and the basis of measurement of income for financial reporting purposes – net			-
Income taxes in different tax rates			
Other	55	(74)	(8)
Taxes on income for the reported year	21,647	14,966	14,345

f. Tax Assessments

The Company and its Israeli subsidiaries have received final tax assessments through the year 2009.

NOTE 13 –TAXES ON INCOME (continued):

g. Effect of adoption of IFRS in Israel on tax liability

As mentioned in note 2a, the Group prepares its financial statements in accordance with IFRS.
As also indicated in the said note, IFRS vary from Accounting Principles Generally Accepted in Israel and accordingly, preparation of financial statements in accordance with IFRS may reflect a financial position, results of operations and cash flows that are materially different from the ones presented in financial statements presented in accordance with accounting principles generally accepted in Israel.

In accordance with the law for the amendment of the Income Tax Ordinance (No. 174 – Temporary Order as to Tax Years 2007, 2008 and 2009), 2010 that was passed in the Knesset on January 25, 2010 and published in the official gazette on February, 4, 2010 (hereafter – the amendment to the ordinance), Accounting Standard No. 29 issued by the Israel Accounting Standard Board would not apply upon determining the taxable income for tax purposes in respect of tax years 2007-2011; this would be the case even if the said accounting standard was applied for the said tax years in the financial statements.
The meaning of the amendment to the ordinance is that IFRS would actually not be applied upon computation of the income reported for tax purposes for the said tax years.
On 31 October, 2011 the Government of Israel published a law memorandum in connection with the amendment to the Income Tax Ordinance (hereafter – the law memorandum) resulting from application of IFRS in the financial statements. Generally, the law memorandum adopts IFRS. Nevertheless, the law memorandum suggests making several amendments to the Income Tax Ordinance, which will serve to clarify and determine the manner of computation of taxable income for tax purposes in cases where the manner of computation is not clear and IFRS do not comply with the principles of the tax method applied in Israel. At the same time, the law memorandum generally adopts IFRS. The legislation procedures relating to the law memorandum have not yet been completed and it is doubtful whether they shall be completed in the near future.
Since the legislation procedures relating to the law memorandum have not yet been completed the Company estimates that the term of the temporary order which applies to the years 2007 to 2013 shall be extended to 2014 as well. In view of the fact that the temporary order applies to tax years 2007 to 2013 as above and in view of the potential extension of the term of the temporary order to 2014, the Group's management expects that at this stage the new legislation shall not apply to tax years preceding 2015.

NOTE 14 – LIABILITIES SECURED BY PLEDGES AND RESTRICTIONS PLACED IN RESPECT OF LIABILITIES:

a. To secure borrowings and long-term loans received by a US subsidiary, this subsidiary recorded a charge on current inventory and trade receivables.

b. To secure long-term loans and other services received by subsidiaries in Israel and the UK, the subsidiary in Israel and subsidiary in the UK recorded a negative pledge on their assets.

c. To secure the long-term loan extended by Bank Leumi Ltd. Bank Leumi Ltd. in the USA, the First International Bank of Israel Ltd. and by two Swiss banks the Group has undertaken upon itself to meet the following financial criteria:
   1) The amount representing the Group's equity would not be lower than $300 million at any given time. As of 31.12.2014 the Group's equity amounts to $ 522,019 thousands.
   2) The amount representing the Group's equity would not be lower than 35% of total assets. As of 31 December, 2014, the Company's equity equals 55.5% of total Company balance sheet.
   3) The ratio between the total financial liabilities of the Group and its operating profit before tax expenses with the addition of depreciation and amortization would not exceed 4.25. As of 31 December, 2014 the said ratio is 1.1.

d. To secure borrowings and banking services received from Bank Leumi Ltd. and the First International Bank of Israel Ltd., the Company has undertaken to meet the following restrictions regarding dividend distribution. The Company shall be allowed to distribute as dividend:

   1) Up to 50% of the retained earnings accumulated through 31 December 2011; based on the retained earnings balance recorded in the Company's balance sheet as of 31 December 2011.

   2) Up to 50% of the Company's net income for each calendar year based on the net income data recorded in the Company's statement of income for the calendar year during which the said income was accumulated.

e. To secure a long-term loan received by a Swiss subsidiary, the Swiss subsidiary and its subsidiaries recorded a negative pledge on their assets.

f. To secure a long-term loan extended by two Swiss banks, the Swiss subsidiary has undertaken to meet the following financial covenants to be computed on the basis of the consolidated financial statements of the subsidiary and all the companies it owns (hereafter – the Swiss group):

   1) The ratio between debt net of cash and EBITDA shall not exceed 3. As of 31 December 2014, the ratio was 1.19.

   2) The amount of equity shall not be lower than 35% of total balance sheet of the Swiss group. As of 31 December 2014 the ratio was 39.8%.

As mentioned above, as of 31 December 2014, the Group meets its obligations.

NOTE 15 – ACCOUNTS RECEIVABLE:

	December 31	
	2014	**2013**
	U.S. dollars in thousands	
a. Trade – composed as follows:		
Open accounts	139,021	136,065
Cheques collectible	1,408	2,308
	140,429	138,373
The item includes – provision for doubtful accounts	5,906	6,076

As of 31 December, 2014 certain trade receivable balances– amounting to $ 28,523 thousands (2013 - $ 26,870 thousands) are in arrears of up to 120 days after date in which payment was due. A provision for doubtful account in the total amount of $149 thousand (2013 - $ 1,318 thousands) was made in respect of it of those balances.

Those balances include the accounts of a large number of customers, in respect of which the Company has not encountered lately any collection problems. The carrying amount of accounts receivable is a reasonable approximation of their fair value since the effect of discounting is immaterial.

The aging analysis of these trade-receivable balances is as follows:

	December 31	
	2014	**2013**
	U.S. dollars in thousands	
Through 90 days	27,431	25,414
90 to 120 days	1,092	1,456
	28,523	26,870
Provision for doubtful accounts	(149)	(1,318)
	28,374	25,552

As of 31 December, 2014, the Company made a provision for doubtful accounts in respect of balances in the total amount of $6,081 thousand (2013 – $5,126 thousand) in arrears of more than 120 days. The amount of the provision as of 31 December, 2014 was $5,724 thousand (2012 – $4,750 thousand).

NOTE 15 – ACCOUNTS RECEIVABLE (continued):

The aging of the said balances is presented below:

	December 31	
	2014	**2013**
	U.S. dollars in thousands	
120 days to 1 year	2,134	1,117
Over 1 year	3,947	4,009
	6,081	5,126
Provision for impairment of receivables	(5,724)	(4,750)
	357	376

Amounts charged to provision for doubtful accounts or released therefrom were included among "selling, marketing, research and development expenses" in the statement of income (see note 20b).

	December 31	
	2014	**2013**
	U.S. dollars in thousands	
b. Other:		
Employees and institutions	440	346
Government institutions	11,771	8,122
Sundry	2,340	3,974
	14,551	12,442

NOTE 16 – INVENTORIES

	December 31	
	2014	**2013**
	U.S. dollars in thousands	
Raw materials and supplies	74,199	71,989
Products in process	11,431	11,453
Finished products	71,193	60,029
	156,823	143,471
Inventories for commercial operations – purchased products	14,277	11,250
	171,100	154,721

NOTE 17 – OTHER

	December 31	
	2014	**2013**
	U.S. dollars in thousands	
Prepaid expenses in respect of operating lease	41	47
Sundry	-	68
	41	115

NOTE 18 – CASH AND CASH EQUIVALENTS:

Classified by currency, linkage terms, the cash and cash equivalents are as follows:

	December 31	
	2014	2013
	U.S. dollars in thousands	
In Dollars	15,387	13,220
In Pounds sterling	4,684	4,627
In Euro	22,184	22,248
In Swiss Francs	1,754	3,297
Yuan	6,516	4,388
NIS	644	467
Guatemalan Quetzal	1,941	-
Peruvian sol	2,054	-
Brazilian real	1,989	2,403
Ruble	3,984	3,537
Other	2,838	3,425
	63,975	57,612

NOTE 19 – ACCOUNTS PAYABLE:

	December 31	
	2014	2013
	U.S. dollars in thousands	
a. Trade:		
Open accounts	59,771	58,407
b. Other:		
Payroll and related expenses	10,787	13,052
Government institutions	15,830	17,704
Provision for commissions and discounts	2,632	3,516
Accrued expenses	11,051	14,719
Provisions	147	166
Conditional consideration in respect of acquisition of subsidiaries	3,061	1,980
Sundry	2,870	1,626
	46,378	52,763

The carrying amount of accounts payables is a reasonable approximation of their fair value since the effect of discounting is immaterial.

NOTE 20 – INCOME STATEMENT ANALYSIS:

	Year ended 31 December		
	2014	**2013**	**2012**
	U.S. dollars in thousands		
a. Cost of Sales:			
Industrial operations:			
Materials consumed	328,175	288,410	279,694
Payroll and related expenses	61,780	53,410	48,763
Depreciation and amortization	13,970	13,327	13,134
Other production expenses	39,837	35,901	32,734
	443,762	391,048	374,325
Decrease (increase) in work in process and finished products inventories	(4,464)	(6,817)	(1,876)
	439,298	384,231	372,449
Commercial operations – cost of products sold	59,697	32,666	19,293
	498,995	416,897	391,742
b. Selling, Marketing, Research and Development Expenses – net:			
Payroll and related expenses	72,820	59,017	54,369
Transportation and shipping	18,005	17,138	16,196
Marketing commissions	10,000	6,471	5,841
Doubtful accounts	1,332	982	(441)
Depreciation and amortization	12,203	9,230	8,510
Travel and entertainment	5,134	4,240	4,015
Office rent and maintenance	5,758	4,641	4,818
Other	15,044	13,504	11,624
	140,296	115,223	104,932
The item includes expenses for product development and research activities, net*	35,708	29,829	28,031
* net of participation from government departments and others	273	182	384

	Year ended 31 December		
	2014	**2013**	**2012**
	U.S. dollars in thousands		
c. General and Administrative Expenses:			
Payroll and related expenses	36,791	30,476	28,852
Depreciation and amortization	4,378	4,442	4,368
Professional fees	4,176	3,860	3,094
Communication, office supplies and Maintenance	5,586	5,319	5,266
Travel and entertainment	1,906	1,927	1,595
Other	7,679	6,107	6,022
	60,516	52,131	49,197

NOTE 20 – INCOME STATEMENT ANALYSIS (continued):

	Year ended 31 December		
	2014	**2013**	**2012**
	U.S. dollars in thousands		
d. Other Expenses (income) – net:			
Capital loss on sale of fixed assets	(147)	(150)	92
Expenses relating to acquisition of subsidiaries	767	918	954
Expenses for site shutdown	164	2,095	-
Other	32	(178)	(35)
Income from bargain purchase	-	-	(1,729)
	816	2,685	(718)
e. Financial Expenses – net:			
In respect of long-term loans and credit	3,446	2,498	5,154
In respect of cash and cash equivalents, short-term deposits and loans, short-term credit and other – net	2,104	3,122	2,038
In respect of exchange differences of trade receivables and trade payable balances – net	(202)	1,908	48
revaluation of put option	4,741	-	-
	10,089	7,528	7,240

NOTE 21 - RELATED PARTIES - TRANSACTIONS AND BALANCES:

a. Transactions with Related Parties:

"Interested parties" - As this term is defined in Israel Securities Regulations (Annual Financial Statements), 2010.
"A related party" - As this term is being defined in IAS 24 - "Related Party Disclosure" (hereafter – IAS 24R).

Key management personnel, who are included together with other officer holders, in the definition of "related party" as per IAS 24R) include the members of the board of directors and the president and CEO of the Company

The main shareholder of the company is ICC Industries Inc. which is holding 36.5% of company shares. The remaining shares are widely held. The controlling shareholder in ICC Industries Inc. is Dr. John Farber – the Chairman of the Board of Directors, who also holds 0.08% of Company's shares.

NOTE 21 – RELATED PARTIES – TRANSACTIONS AND BALANCES (continued):

1) Transactions with the controlling shareholder and its affiliates:

During the ordinary course of business, the Company and its affiliates conduct negligible transactions with the companies affiliated to the controlling shareholder. As part of these transactions, the Company's subsidiary sells to Fallek Chemical Japan, an affiliate of the controlling shareholder, products at market prices for marketing to a specific customer in Japan. In addition, as part of these transactions, the Company purchases from Azur S.A., an affiliate of the controlling shareholder, raw materials at cost prices and production services at market price. These transactions were approved by the Company's Board of Directors and they are considered to be negligible as this term is defined by regulation 41(a)(6)(a) of the Securities Regulations (Annual Financial Reports), 2010.

	2014	**2013**	**2012**
Income (expenses):	**U.S. dollars in thousands**		
Sales – affiliates (companies controlled by the controlling shareholder):			
Fallek Chemical Japan	239	206	574
Other	10	8	4
	249	214	578
Purchases:			
Affiliates (companies controlled by the controlling shareholder):			
Azur S.A	(1,588)	(1,744)	(1,743)
Dividend	(1,733)	(1,439)	(1,132)
Other expenses:			
Affiliates -			
Azur S.A.	(14)	(21)	(42)
Benefits to related parties:			
Wages and salaries	(3,056)	(2,810)	(2,603)
Director fees (in the Company)	(238)	(209)	(186)

2) Shares granted to the President of the Company

On August 20, 2012, the Company's board of directors approved the grant of 275,000 options to the President of the Company; the value of the benefit is computed in accordance with the binomic model and was estimated at $ 434 thousands at date of grant.

On August 19, 2014, the Company's board of directors approved the grant of 137,500 options to the President of the Company; the value of the benefit is computed in accordance with the binomic model and was estimated at $ 521 thousands at date of grant.

NOTE 21 – RELATED PARTIES – TRANSACTIONS AND BALANCES (continued):

The total benefit component granted to the President (see note 12) in the years 2014, 2013 and 2012 as computed at date of grant is $772 thousand, $230 thousand and $806 thousand, respectively.
Benefit costs that have been charged to the income statements, in respect of the said shares granted in the years 2014, 2013 and 2012 are $464 thousand $ 423 thousands and $513 thousand, respectively.

3) Terms of the employment for the President of the Company

On January 14, 2014, the general meeting of the Company's shareholders approved the compensation policy for senior office holders in the Company, including the Company's president; the general assembly approved the compensation policy after it was approved by the compensation committee and the Company's Board of Directors ("compensation policy"). For details regarding the compensation policy see Company's report of December 29, 2013 (reference 2013-01-111694).

Under the compensation policy the components of the president's compensation package include the following:

The terms of employment of the President & CEO include a monthly salary (index-linked), social benefits as is customary in the economy (including executive insurance, education fund, disability insurance, recuperation pay, sick leave and vacation pay), a 13th month salary, other benefits (including mobile phone, landline at home and newspapers), and an executive car. The President & CEO is also entitled to an annual bonus and is allocated options in accordance with the compensation policy that has been approved. The President & CEO’s employment will end 6 months from the date on which the Company serves notice of its desire to end the engagement and 3 months from the date on which The President & CEO notifies the Company of his desire to end the engagement. Should the Company inform Mr. Yehudai of the end of his employment within 12 months of the date from which ICC Handels AG holds less than 26% of the Company's share capital or voting rights, The President & CEO shall be entitled to receive his salary from the Company (save for vacation pay, sick leave, bonuses and options) for a period of 12 months starting at the end of the notice period. In such case The President & CEO will also be entitled to immediately exercise all options previously granted him even if their vesting period has not yet ended. Upon termination of his employment with the Company, The President & CEO is entitled to receive double the amount of severance pay stipulated by law.

4) The articles of incorporation of the company allow insurance coverage to officials in the company as outlined by Israeli legislation. The company applied a policy of indemnifying officers and other officials in subsidiaries. The company decided to buy insurance to officers in relation to their job, subject to the law and other restrictions.

NOTE 21 – RELATED PARTIES – TRANSACTIONS AND BALANCES (continued):

b. Balances with Related Parties:

	31 December		
	2014	**2013**	**2012**
	U.S. dollars in thousands		
1) Current receivables – presented among "other receivables-other" and "trade receivables"			
Affiliated companies:			
Fallek	-	-	342
ICC	2	2	-
	2	2	342
Highest balance during the year	234	342	342
2) Current payables shareholder and related parties:			
Azur S.A.	157	228	18

NOTE 22 – SUBSEQUENT EVENTS

a. **Acquisition of Vitiva**

On February 4, 2015 Frutarom completed the purchase of 92% of the share capital of the Slovenian company VITIVA Proizvodnja in storitve d.d., which grants it the right to acquire 100% of Vitiva's share capital, in exchange for a cash payment of approximately USD 10.0 million.

Vitiva specializes in the research and development, production, marketing and sales of specialty natural extracts from plants exhibiting antioxidant activity or scientifically proven health attributes backed up by clinical studies and of natural colors for customers in the food, pharmaceutical, nutraceutical, and cosmetics markets. Among its customers are some of the world's top food, pharmaceutical, and cosmetics manufacturers. Vitiva's revenues grew from USD 8.7 million in 2013 to approximately USD 11 million for the 12-month period ending November 2014 (a 27% increase). Its activity will be integrated into Frutarom's Specialty Fine Ingredients division.

Vitiva has many years of experience and excellent capabilities in extracting active elements from plants (particularly rosemary, olive and citrus, among others) and this will help Frutarom expand its portfolio of natural products for the food industry as well as in the fields of health and cosmetics. In addition, Vitiva has R&D abilities and a pool of knowledge based on longstanding research for continuing to expand its current product portfolio and toward entry into other fields such as the field of pet food and livestock feed preservation. Combining these abilities with Frutarom's capabilities in the field of antioxidants, particularly in the area of food preservation and protection and lengthening shelf life based on natural ingredients, will further strengthen Frutarom's position as a leading player in R&D, production, and sales for these types of solutions. The natural food colors activity will join the natural food colors activity by Montana Food, advancing the implementation of Frutarom's strategy for penetrating this burgeoning field with the intention of continuing to invest in a major expansion of its global activity in this growing area.

NOTE 22 – SUBSEQUENT EVENTS (continued):

b. **Acquisition of FoodBlenders**

On February 3, 2015 Frutarom purchased 100% of the shares of UK-based FoodBlenders Limited for a cash payment of approximately USD 2.4 million plus, conditional on performance, an additional payment expected to stand at about USD 0.6 million.

FoodBlenders, founded in 1998, engages in the development, manufacture and marketing of savory flavor solutions which mainly include spice and seasoning mixes, functional ingredients, marinades and sauces for the food industry, with particular emphasis on the convenience foods segment. In 2014 FoodBlenders posted sales totaling approximately USD 3 million. FoodBlenders develops, manufactures and markets its products at a site in England not far from the Frutarom site at Wellingborough, and has a wide customer base which includes British food and private label manufacturers. FoodBlenders' product line and technologies complement the product portfolios and activities of UK-based Savoury Flavours and EAFI which were acquired by Frutarom in 2012 and 2011 respectively and which also specialize in savory flavor solutions. The proximity to the Frutarom site at Wellingborough and the complementary line of products promise to generate significant synergies between FoodBlenders' activity and Frutarom's expanding savory activity in the UK and throughout the world.

c. **Acquisition of Ingredientes Naturales Seleccionados**

On February 3, 2015 Frutarom purchased 100% of the share capital of the Spanish company Ingredientes Naturales Seleccionados ("Ingrenat") in exchange for approximately USD 8 million plus an additional amount of approximately USD 1.1 million depending on Ingrenat's performance in 2015.

Ingrenat specializes in the research and development, production, and sales and marketing of natural extracts from plants including, among others, paprika, rosemary, bixin, alfalfa, and more, which deliver taste, color, and antioxidant activity solutions for the food industry. Numbering among its customers are food manufacturers and leading flavor, fragrance, and natural color producers. Ingrenat's sales grew 10% in 2014 to approximately USD 9.8 million. The value of its net assets (not including cash or debt) in 2014 stood at approximately USD 6.9 million. Ingrenat's operations will be integrated into the activities of Frutarom's Specialty Fine Ingredients division with which they share similar profitability margins.

The acquisition of Ingrenat is a continuation of the implementation of Frutarom's strategy of deepening and expanding its activity in the growing field of natural food colors and antioxidants, and it will continue investing towards substantially expanding its global activity in this important and growing area. The natural food colors activity joins the natural colors activity of Montana Food, which was acquired in October 2014, and of Vitiva for which a purchase agreement was signed in December 2014 and the transaction was completed in February. Ingrenat's activity in antioxidants based on natural substances, particularly in the field of food preservation and protection and extension of shelf life, further reinforces Frutarom's line of solutions in this area that also gained a substantial boost with the acquisition of Vitiva which has activity in this growing field as well.

NOTE 22 – SUBSEQUENT EVENTS (continued):

d. **Distribution of dividend**

On March 15, 2015 the Company's Board of Directors declared the distribution of a dividend of NIS 0.38 per share. Total amount of the dividend is $5,552 thousand (based on exchange rate as of date of confirmation of these financial statements).

NOTE 23 – LIST OF MATERIAL CONSOLIDATED SUBSIDIARIES AND INVESMENT IN SUBSIDIARIES

a) LIST OF MATERIAL CONSOLIDATED SUBSIDIARIES

Name of company	Percentage of shareholding and control	
	31 December	
	2014	2013
	%	%
Subsidiaries:		
Frutarom Ltd.	100	100
Frutarom Switzerland Ltd.	100	100
Frutarom (UK) Ltd.	100	100
Frutarom U.S.A. Inc.	100	100
Frutarom Savory Solutions GmbH	100	100
Frutarom Etol Tovarna arom in etericnih d.o.o.	100	100
Vantodio Holdings Limited	75	75
Frutarom Italy S.R.L	100	100
Frutarom Germany GmbH	100	100
Frutarom Belgium N.V	100	100
Frutarum Peru	100	100

b) INVESMENT IN SUBSIDIARY HELD DIRECTLY BY THE COMPANY

Name of the subsidiary	State of Incorporation	Percentage of shareholding	The value of the investment	Capital notes
			31 December 2014	
			U.S. dollars in thousands	
Frutarom Ltd.	Israel	100%	412,873	100,858

SECTION D

ADDITIONAL INFORMATION

D

Chapter D – Additional Information on the Corporation

Company name:	**Frutarom Industries Ltd.**
Registration number:	**52-004280-5**
Address:	**25 HaShaish St., Haifa Bay** **P.O.B. 10067, 2611001**
Email:	**info@frutarom.com**
Telephone:	**+972-4-846 2449**
Fax:	**+972-4-872 2517**
Balance Sheet date:	**December 31, 2014**
Date of report:	**March 15, 2015**
Period of report:	**January 1, 2014 - December 31, 2014**

Regulation 10A - Summary of Quarterly Profit and Loss Reports

Following is a summary of the of the corporation's overall P&L statement for each calendar quarter of the reported year:

IN US$ 000s	Q1 – 2014		Q2 - 2014		Q3 - 2014		Q4 - 2014		2014 Total	
SALES	**188,467**	**100.0%**	**218,081**	**100.0%**	**210,755**	**100.0%**	**202,244**	**100.0%**	**819,547**	**100.0%**
Cost of sales										
Material consumed	86,605	46.0%	103,423	47.4%	101,853	48.3%	98,002	48.5%	389,883	47.6%
Other manufacturing	28,322	15.0%	28,770	13.2%	27,333	13.0%	24,687	12.2%	109,112	13.3%
Total	**114,927**	**61.0%**	**132,193**	**60.6%**	**129,186**	**61.3%**	**122,689**	**60.7%**	**498,995**	**60.9%**
GROSS PROFIT	**73,540**	**39.0%**	**85,888**	**39.4%**	**81,569**	**38.7%**	**79,555**	**39.3%**	**320,552**	**39.1%**
R&D, Selling and G&A										
R&D		-		-		-		-		-
Selling expenses	34,713	18.4%	34,628	15.9%	36,268	17.2%	34,687	17.2%	140,296	17.1%
General & Administration	14,822	7.9%	15,746	7.2%	14,287	6.8%	15,661	7.7%	60,516	7.4%
Other expenses	72	0.0%	190	0.1%	68	0.0%	486	0.2%	816	0.1%
Total	**49,607**	**26.3%**	**50,564**	**23.2%**	**50,623**	**24.0%**	**50,834**	**24.9%**	**201,628**	**24.6%**
OPERATING PROFIT	**23,933**	**12.7%**	**35,324**	**16.2%**	**30,946**	**14.7%**	**28,721**	**14.4%**	**118,924**	**14.5%**
Financing expenses	1,420	0.8%	1,570	0.7%	1,335	0.6%	5,966	2.9%	10,291	1.3%
Translation (gain) losses	40	0.0%	703	0.3%	(553)	(0.3)%	(392)	(0.2)%	(202)	(0.0)%
Total	1,460	0.8%	2,273	1.0%	782	0.4%	5,574	2.8%	10,089	1.2%
PROFIT BEFORE TAX	**22,473**	**11.9%**	**33,051**	**15.2%**	**30,164**	**14.3%**	**23,147**	**11.4%**	**108,835**	**13.3%**
TAX	4,193	2.2%	7,571	3.5%	5,994	2.8%	3,461	1.7%	21,219	2.6%
Tax rate	18.7%		22.9%		19.9%		15.0%		19.5%	
NET PROFIT	**18,280**	**9.7%**	**25,480**	**11.7%**	**24,170**	**11.5%**	**19,686**	**9.7%**	**87,616**	**10.7%**

Regulation 10C - Use of Securities' Proceeds

Not relevant.

Regulation 11 – List of Investments in Subsidiaries and Affiliates

					Holding %		
Name of company	Type of Share	Par Value	Number of Shares	Total Par Value	Equity	Voting	Right to appoint directors
Frutarom Ltd.* 51-013293-9	Ordinary	NIS 1	23,972,645	23,972,645	100	100	100

All other companies in the Frutarom Group are held through Frutarom Ltd., directly or indirectly. For further details regarding the consolidated companies in the Frutarom Group and holdings in them, see Note 23 to the Company's financial statements of December 31, 2014.

Regulation 12 - Changes in Investments in Subsidiaries and Affiliates

A. Montana Food

On November 28, 2014 the Company completed the acquisition of the flavors and natural food colors division of the Peruvian company Montana S.A in exchange for a cash payment of approximately US$ 25 million and the assumption of approximately US$ 7 million of debt.

For further details regarding the acquisition see the Company's immediate reports dated September 30, 2014, October 14, 2014 and November 29, 2014.

B. VITIVA proizvodnja in storitve d.d

After the balance sheet date, on February 4, 2015, Frutarom completed the acquisition of 92% of the share capital of Vitiva, which gives it the right to acquire 100% of Vitiva's share capital, in exchange for a cash payment of approximately US$ 10.0 million, and this in accordance with an agreement signed on December 23, 2014. The acquisition was funded using independent sources.

C. Ingredientes Naturales Seleccionados S.L.

After the balance sheet date, on February 2, 2015, Frutarom acquired 100% of the share capital of the Spanish company Ingredientes Naturales Seleccionados S.L. ("**Ingrenat**") in exchange for payment of approximately US$ 8 million (€ 7 million) plus an additional sum of up to US$ 1.1 million (€ 1 million) contingent on Ingrenat's performance during 2015. The acquisition was funded through bank financing.

For further details regarding the acquisition see the Company's immediate report dated February 3, 2015.

D. <u>FoodBlenders</u>
After the balance sheet date, on February 3, 2015, Frutarom acquired 100% of the share capital of the UK company FoodBlenders in return for payment of approximately US$ 2.4 million (£ 1.6 million) plus, contingent on future performance, an additional sum expected to stand at approximately US$ 600,000 (£ 400,000). The acquisition was funded using independent sources.

For further details regarding the acquisition see the Company's immediate report dated February 3, 2015.

For further details regarding the subsidiaries in the Frutarom Group see Note 23 to the Company's financial statements of December 31, 2014.

Regulation 13 - Income of and from Subsidiaries and Affiliates

<table>
<tr><th rowspan="2">Company name</th><th rowspan="2">Profit (loss) for the reporting period (US$ 000)</th><th rowspan="2">Other profit (loss) (US$ 000)</th><th rowspan="2">Total profit (loss) for the reporting period</th><th colspan="2">Dividend (US$ 000)</th><th colspan="2">Management fee (US$ 000)</th><th colspan="2">Interest</th></tr>
<tr><th>Until the reporting date</th><th>After the reporting date</th><th>Until the reporting date</th><th>After the reporting date</th><th>Until the reporting date</th><th>After the reporting date</th></tr>
<tr><td>Frutarom Ltd.</td><td>96,585</td><td>(83,611)</td><td>12,974</td><td>4,712</td><td>-</td><td>-</td><td>-</td><td>-</td><td>-</td></tr>
</table>

Regulation 14 – Loans

Granting loans is not one of the Group's main business activities.

Regulation 20 - Trading on Stock Exchange

During the reporting period the Company issued 152,000 additional ordinary shares of NIS 1 par value each upon the exercise of stock options by Company employees.

There were never any suspensions in the trading of the Company's shares during the reporting period.

Regulation 21 –Payments to Interested Parties and Senior Officeholders

Section (a) (1)

Following is a breakdown of remuneration noted in the Company's financial statements for the period ended December 31, 2014 to each of the five highest paid senior officeholders of the Company or a corporation under its control and provided to them in connection with their position in the Company or a corporation under its control:

Details of Officeholder				Remuneration for Services [1]							Other Payments			Total [1]
Name	Position	% Position	% of Holdings [2]	Salary [3]	Bonus [4]	Shares' Based Payment [5]	Manage-ment Fees	Consu-lting Fees	Comm-ission	Other	Interest	Rent	Other	
Ori Yehudai	President & CEO [6]	100%	1.97% [7]	725	1,620	459 [8]	-	-	-	-	-	-	-	3,056
Amos Anatot	EVP – Supply Chain [9]	100%	0.26% [10]	224	130	130 [11]								546
Alon Granot	EVP & CFO [12]	100%	0.28% [13]	216	129	126 [14]	-	-	-	-	-	-	-	534
Tali Mirsky Lachman	Global VP – Legal & Company Secretary [15]	100%	0.12% [16]	156	56	69 [17]	-	-	-	-	-	-	-	342
Guy Gill	VP – Finance [18]	100%	0.13% [19]	133	54	64 [20]	-	-	-	-	-	-	-	300

Notes to the table above:
[1] Remuneration reflects cost to the Company. Amounts are in US$ thousands.
[2] On a fully diluted basis as at the date of this report.
[3] Including fringe benefits (car maintenance, telephone, social benefits, provisions for termination of employment and any other payment made to the senior officeholders).
[4] The size of bonuses to senior officeholders were determined in accordance with the compensation policy and approved by the Company's Board of Directors.
[5] The amounts in the table reflect the benefit component for the options granted under the 2003 Plan, the 2012 Plan and the 2010 Plan (for allocations performed from 2008 through 2014) as recognized in the Company's 2014 Financial Statements.
For further details on the Company's option plans see Note 12 to the Company's Financial Statements for December 31, 2014.
[6] Mr. Yehudai has been employed with the Company since 1986, and in 1996 began serving as its President and CEO. Mr. Yehudai's terms of employment include a monthly salary (index-linked), social benefits as is customary in the economy (including executive insurance, study fund, disability insurance, recuperation pay, sick leave and vacation pay), a 13th month salary, other benefits (including mobile phone, landline at home and newspapers), and an executive car. Mr. Yehudai is also entitled to an annual bonus and is allocated options in accordance with the Company's options plans as specified in sections (7) and (8) below. (For details on the approved Compensation Policy see the Company's report on this subject from December 29, 2013). Mr. Yehudai's employment may end 6 months from the date on which the Company serves notice of its desire to end the engagement and 3 months from the date on which Mr. Yehudai notifies the Company of his desire to end the engagement. Should the Company inform Mr. Yehudai of the end of his employment within 12 months of the date from which ICC Handels AG holds less than 26% of the Company's share capital or voting rights, Mr. Yehudai shall be entitled to receive his salary from the Company (save for vacation pay, sick leave, bonuses and options) for a period of 12 months starting at the end of the notice period. In such case Mr. Yehudai will also be entitled to immediately exercise all options previously granted him even if their vesting period has not yet ended. Upon termination of his employment with the Company, Mr. Yehudai is entitled to receive double the amount of severance pay stipulated by law whenever his employment with the Company ends.
[7] As of December 31, 2014 Mr. Yehudai held 696,821 options exercisable into 696,821 of the Company's ordinary shares.
[8] As at the date of this report, the balance of options granted to Mr. Yehudai under the 2003 Plan is 9,457, the balance of options granted to Mr. Yehudai under the 2012 Plan is 91,525, and the balance of options granted to Mr. Yehudai under the 2010 plan is 595,839. As stated above, beginning in 2013 the options granted under the 2012 Plan are part of the deferred equity component of the annual bonus.
[9] Mr. Anatot has been employed with the Company since 2010. Mr. Anatot's terms of employment include a monthly salary, social benefits as is customary in the economy (including executive insurance, education fund, disability insurance, recuperation pay, sick leave and vacation pay), an annual bonus at the Company's discretion, a mobile phone and a vehicle. He is also allocated options according to the Company's options

plans as specified in sections (10) and (11) below. The engagement between the sides will end three months from the date on which either side serves notice on the other of a desire to end the engagement. Should the Company inform Mr. Anatot of the end of his employment with the Company within 12 months of the date from which ICC Handels AG holds less than 26% of the Company's share capital or voting rights, Mr. Anatot shall be entitled to receive his salary from the Company (save for vacation pay, sick leave, bonuses and options) for a period of six months from the end of such notice period. In such case Mr. Anatot will also be entitled to immediately exercise all options previously granted him even if their vesting period has not yet ended.

[10] As of December 31, 2014 Mr. Anatot held 152,983 options exercisable into 152,983 of the Company's ordinary shares.

[11] As of the date of this report, the balance of options granted to Mr. Anatot under the 2012 Plan is 28,313 and the balance of options granted to Mr. Anatot under the 2010 Plan is 124,670.

[12] Mr. Granot has been employed with the Company since 2001. Mr. Granot’s terms of employment include a monthly salary, social benefits as is customary in the economy (including executive insurance, education fund, disability insurance, recuperation pay, sick leave and vacation pay), a 13th month salary, an annual bonus at the Company's discretion, other benefits (including mobile phone, newspapers, and a landline at home), plus a vehicle. He is also allocated options according to the Company’s options plans as specified in sections (13) and (14) below. Mr. Granot’s employment will end upon three months from the date on which either side serves notice on the other of a desire to end the engagement. Should the Company inform Mr. Granot of the end of his employment with the Company within 12 months of the date from which ICC Handels AG holds less than 26% of the Company's share capital or voting rights, Mr. Granot shall be entitled to receive his salary from the Company (save for vacation pay, sick leave, bonuses and options) for a period of six months from the end of such notice period. In such case Mr. Granot will also be entitled to immediately exercise all options previously granted him even if their vesting period has not yet ended.

[13] As of December 31, 2014 Mr. Granot held 165,577 options exercisable into 165,577 ordinary Company shares.

[14] As of the date of this report the balance of options granted to Mr. Granot under the 2003 Plan is 1,752, the balance of the options granted to Mr. Granot under the 2012 Plan is 26,325 and the balance of options granted to Mr. Granot under the 2010 plan is 137,500.

[15] Ms. Mirsky has been employed with the Company since 2010. Ms. Mirsky’s terms of employment include monthly salary, social benefits as is customary in the industry (including managers’ insurance, education fund, insurance for loss of work capacity, recuperation pay, sick days and vacation days), an annual bonus, an acclimation bonus, a mobile phone and a vehicle. In addition, Ms. Mirsky is being granted options according to the Company’s option plans, as detailed in sections (16) and (17) below. Ms. Mirsky’s employment may be terminated with 3 months advance written notice given by either party. In the event a notice of termination is delivered to Ms. Mirsky by the Company within 12 months following the date upon which ICC Handels AG’s holding (directly or indirectly) fall below 26% of the issued and paid up capital of the Company or the voting

rights in the Company, all options previously granted to Ms. Mirsky will become immediately exercisable, even if they vesting period has not been completed.

[16] As of December 31, 2014 Ms. Mirsky held 70,467 options exercisable into 70,467 ordinary shares of the Company.

[17] As of the date of this report, the balance of options granted to Ms. Mirsky under the 2012 Plan is 10,466 and the balance of options granted to Ms. Mirsky under the 2010 Plan is 60,001.

[18] Mr. Gill has been employed with the Company since 2006. Mr. Gill's terms of employment include a monthly salary, social benefits as is customary in the economy (including executive insurance, education fund, disability insurance, recuperation pay, sick leave and vacation pay), an annual bonus at the Company's discretion, a mobile phone and a vehicle. He is also allocated options according to the Company's options plans as specified in sections (19) and (20) below. The engagement between the sides shall end three months from the date on which either side serves notice on the other of a desire to end the engagement.

[19] As of December 31, 2014 Mr. Gill held 80,630 options exercisable into 80,630 ordinary Company shares.

[20] As of the date of this report, the balance of options granted to Mr. Gill under the 2012 Plan is 7,296 and the balance of options granted to Mr. Gill under the 2010 Plan is 73,334.

Section (a)(2)

There are no senior officeholders in the corporation receiving higher remuneration who are not included in the above table.

Section (a)(3)

There are no interested parties in the corporation who received remuneration not mentioned in the above table, except for directors. The remuneration paid to all of the directors in 2014, which does not deviate from the customary directors' remuneration, came to a total of US$ 238 thousand.

Section (b)

No remuneration has been given to senior officeholders after the reporting period and prior to the submission of this report in connection with their service or employment in the reporting period which were not recognized in the Financial Statements for the reporting period.

Regulation 21A – Control of the Corporation

The principal shareholder in the Corporation is ICC Industries Inc., via its subsidiaries. The principal shareholders of ICC Industries Inc. are Dr. John J. Farber and Mrs. Maya Farber.

<u>Regulation 22- Transactions with Controlling Parties</u>

Following are details, to the best of the Company's knowledge, of any transaction with the controlling shareholder or in which the controlling shareholder has personal interest in its approval, in which the Group engaged in 2014 or later, through the date of publication of this report or which is still valid at the time of the publication of the report:

<u>Transactions included in Section 270(4) of the Companies Law, 1999 (the "**Companies Law**")</u>

(a) According to a resolution of the Company's Board of Directors from February 9, 2011, passed after having been approved by the Audit Committee, starting as of February 10, 2011 an annual remuneration and participation remuneration will be paid to the Company's directors (including external directors and directors who are controlling shareholders or relatives of controlling shareholders) in amounts equivalent to the fixed amount prescribed under the Companies Regulations (Rules Regarding Remuneration to External Directors) 2001 (the "Remuneration Regulations"), according to the Company level as may be from time to time.

(b) The Company's annual general meeting of shareholders held on June 10, 2012 resolved as follows:

- **Amendment of the Company Articles**

  Amendment of the Company's Articles of Association in a manner adapting them to the updated wording of the Companies Law and of the Efficiency of Enforcement Proceeding of the Securities Authority (Legislation Amendments) Law, 2011 ("**Administrative Enforcement Law**"), allowing, inter alia, insurance and indemnification of officeholders and directors in connection with expenses of administrative enforcement processes and payment to injured parties, as prescribed under sections 56H and 52[52](A)(1)(a) to the Securities Law, 1968 (hereinafter: "**Administrative Enforcement Payments**" and the "**Securities Law**", accordingly).

- **Granting undertakings for indemnification of directors who are controlling shareholders or relatives thereof, for a period of three years.**

  To approve granting undertakings for indemnification of directors who are controlling shareholders or relatives thereof, for a period of three years.

- **Purchase of insurance policies for directors who are controlling shareholders or relatives thereof**

  Approval of the Company's engagement under the directors' insurance policy for directors who are controlling shareholders or their relatives under conditions identical to those given to directors who are not controlling shareholders or their relatives, as have been from time to time, for a period of three years.

For further details regarding the above transactions see the Company's report on the General Meeting of May 13, 2012 and June 11, 2012.

(c) The Company's annual general meeting, held on January 14, 2014, resolved the following:

- **Approval of the Compensation Policy**
  For details regarding the Compensation Policy approved, see the Company's report on the matter dated December 29, 2013.
- **Purchase of Insurance for Directors and Officeholders who are not controlling shareholders or relatives of such**
  Approval of the purchase of insurance for directors and officeholders who are not controlling shareholders or their relatives, for a period of three years from the date of approval of this resolution, or until the annual general meeting to be held in 2016, the later of the two. The amount of coverage will not exceed US$ 80 million, and the annual premium to be paid for said policy will not exceed US$ 200,000 (no change from the current approved premium ceiling). The terms of the policy to be purchased will be those customary in the market with regard to the Company, the nature of its activities and its exposures.

<u>Transactions not included in Section 270(4) of the Companies Law</u>

During its ordinary course of business, the Group executes negligible transactions with companies under the controlling shareholder's control. As part of these transactions, the Company's subsidiary sells products to a company controlled by the controlling shareholder for marketing to a specific customer in Japan. In the framework of these transactions, the Company also purchases raw materials from a company controlled by the controlling shareholder at cost, as well as production services at market price. For more information regarding the above transactions, see Note 21 of the Financial Reports.

Transactions are classified as negligible in accordance with the approval of the Board of Directors dated January 17, 2011, setting guidelines and rules for the classification of a transaction of the Company or of its consolidated or related company with an interested party as negligible ("**Negligibility Procedure**"). According to the above resolution, the Company follows these guidelines in order to examine the extent of the Company's disclosure in the periodic reports and the prospectus, including shelf proposal reports, with regards to transactions with interested parties as set out in regulation 41(A)(6)(a) of the Securities Regulations (Annual Financial Reports), 2010 ("**Financial Reports Regulations**") and with regards to transactions with controlling shareholders or such that a shareholder has a personal interest in their approval, as stated in regulation 22 of the Securities Regulations (Immediate and Periodic Reports), 1970 ("**Periodic Reports Regulations**") and in regulation 54 of the Securities Regulations (Prospectus' details, draft, shape and form), 1969, and to examine the need to issue an immediate report on the stated transactions, as set out in regulation 37a(6) of the Periodic Reports Regulations. For details on the Negligibility Procedure, see the Company's Immediate Report dated January 18, 2011.

Regulation 24 - Convertible Shares and Securities Held by Interested Parties

For details regarding holdings of interested parties in the Company see the immediate report on the status of holdings of interested parties and senior officeholders published on March 5, 2015. To the best of the Company's knowledge, there have been no material changes in interested parties' holdings since the date referred to in this status report.

Regulation 24A – Registered and Issued Share Capital and Convertible Securities

As at the date of this report, the Company's registered share capital is NIS 100,000,000 divided into 100,000,000 shares of NIS 1 par value each.

As at the date of this report, the Company's issued share capital is: NIS 58,660,845 divided into 58,660,845 shares of NIS 1 par value each.

Issued share capital after deduction of dormant shares: NIS 58,347,451 divided into 58,347,451 shares of NIS 1 par value each.

As of the date of this report the Company holds 313,394 of its shares in accordance with the Company's 2003 Plan and 2012 Plan. These shares are dormant shares under Section 308(A) to the Companies Law, and therefore do not confer any rights.

As at December 31, 2014 the balance of options existing under the option plan which the Board of Directors adopted in 2003, 2010 and 2012 is 21,138, 1,298,012 and 293,202 respectively. For further details regarding the above option plans, see regulation 21 above and Note 12 to the Company's Financial Statements

Regulation 24B - Registry of the Company's Shareholders

For the updated registry of the Company's shareholders, see the Company's immediate report dated December 21, 2014.

Regulation 25A – Registered Office

Registered office:	25 HaShaish St., P.O.B. 10067, Haifa Bay 2611001, Israel
Email:	info@frutarom.com
Telephone:	+972 4 846 2402
Fax:	+972 4 872 2517

Regulation 26 – Members of the Board of Directors

Name of Director	Dr. John J. Farber, Chairman	Maya Farber	Sandra Farber	Hans Abderhalden
ID \Passport no.	520850285 (US Passport)	520777916 (US Passport)	453588940 (US Passport)	x4983003 (Swiss)
DOB	1925	1936	1957	1939
Address for service of court processes	435 E. 52 St., New York, N.Y. 10022, U.S.A.	435 E. 52 St., New York, N.Y. 10022, U.S.A.	340 Riverside Drive, New York, N.Y. 10025 US	Lerchenbergstrasse 114, 8703 Erlenbach 8703, Switzerland
Nationality	U.S.A.	U.S.A.	U.S.A.	Swiss
Member of BOD committees	No	No	Was a member of the Compensation Committee until November 26, 2012	No
Independent \ external director	No	No	No	No
Director with financial and accounting expertise or professional capacity	Financial and Accounting Expertise and Professional Capacity	Professional Capacity	Professional Capacity	Financial and Accounting Expertise and Professional Capacity
Company , subsidiary or related company employee or interested party	Chairman of ICC Industries Inc., the Company's controlling shareholder	No	Vice-Chair of ICC Industries Inc.	No
Year began serving as director	1996	1996	2011	2004
Education	Ph.D. in Chemistry from Polytechnic Institute of Brooklyn, New York	Hunter College, New York and Art Students' League	Juris Doctor, New York University School of Law	IMD Program for Executive Development from IMD, Switzerland
Occupation over past five years	Chairman of the Board of the Company and of ICC Industries Inc.	Artist	Vice-Chair of ICC Industries Inc.	Director in Frutarom Switzerland Ltd. and advisor

Names of corporations where serves as director	Chairman of the Board of ICC Industries Inc. And serves as Director in ICC Industries Inc. subsidiaries	ICC Industries Inc.	Vice-Chair of ICC Industries Inc. and director in ICC subsidiaries	Served as Director in Frutarom Switzerland Ltd. until August 2013
Relative of other Interested party in the corporation	Married to Ms. Maya Farber and father of Ms. Sandra Farber, both directors in the Company	Married to Dr. John J. Farber, Chairman of the Board and the mother of Ms. Sandra Farber, director in the Company	Daughter of Dr. John J. Farber, the Chairman of the Board and Ms. Maya Farber, director in the Company	No
Accounting and financial expertise for purposes of minimal no. of directors under section 92(A)(12) to the Companies Ordinance	Yes	No	No	Yes

Name of Director	Isaac Angel	Yacov Elinav	Gil Leidner	Dafna Sharir
ID \Passport no.	012735478 (Israeli)	006287338 (Israeli)	50776889 (Israeli)	23761455 (Israeli)
DOB	1956	1944	1951	1968
Address for service of court processes	2A Zahal St., Tel Aviv	10 Hadudaim St., Herzliya	3 Ha'aliya St., Beit Yitzhak, 42920	17 Rabina St., Tel Aviv
Nationality	Israeli	Israeli	Israeli	Israeli
Member of BOD committees	Member of the Board's Audit Committee, Balance Sheet Committee and Compensation Committee	Member of the Board's Audit Committee, Balance Sheet Committee and Compensation Committee	Member of the Board's Audit Committee, Balance Sheet Committee and Compensation Committee	Member of the Board's Audit Committee and Compensation Committee
Independent \ external director	External director	External director	Independent director	External director
Director with financial and accounting expertise or professional capacity	Financial and Accounting Expertise and Professional Capacity	Financial and Accounting Expertise and Professional Capacity	Financial and Accounting Expertise and Professional Capacity	Financial and Accounting Expertise and Professional Capacity
Company , subsidiary or related company employee or interested party	No	No	No	No
Year began serving as director	2008	2008	2010	2014
Education	High school	BA in economics and business management, the Hebrew University, Jerusalem	LLB, Tel Aviv University	MBA from Insead, LLM New York University, LLB Tel Aviv University, BA in economics, Tel Aviv University

Occupation over past five years	Business advisor, CEO Ormat Technologies starting July 1, 2014	Chairman of the board of Dash Provident Fund Management Ltd., Chairman of Yellow Pages Ltd., Chairman of the Bank for Industrial Development Israel Ltd.	Managing partner at Galram Consultants	Consultant on mergers and acquisitions (2008-2010), member of the board of directors at Ormat Industries Ltd.
Names of corporations where serves as director	Did not serve as director at any other corporation during the reported year and as of the date of this report's release.	Yellow Pages Ltd.; Elinav Consulting and Services Ltd.; Sapiens Ltd.; Polar Communication Ltd.; Ofer Investments Ltd; Global Box Ltd.; Excellence Provident Funds Ltd.; Tadir-Gan Ltd.	Member of the Management Committee of the Research Fund of Tel Aviv Sourasky Medical Center	Served as a director at Ormat Industries Ltd. until February 2015.
Relative of other Interested party in the corporation	No	No	No	No
Accounting and financial expertise for purposes of minimal no. of directors under section 92(A)(12) to the Companies Ordinance	Yes	Yes	Yes	Yes

Regulation 26A - Senior Officeholders

Name of officeholder	**Ori Yehudai**	**Alon Granot**	**Amos Anatot**
Position in corporation, subsidiary, related company or interested party	President and CEO. Serves as director in Frutarom subsidiaries.	Executive Vice President and CFO. Serves as director in Frutarom subsidiaries and as the Group's officer responsible for managing market risks.	Executive Vice President Global Supply Chain and Operations. Serves as director in Frutarom subsidiaries.
ID no.	052731569	057210247	51923548
DOB	1954	1961	1953
Year began serving in the company	President and CEO as of 1996 (first began working for the Company in 1986)	2001	2010
Independent authorized signatory	No	No	No
Interested party in the corporation or relative of senior officeholder or of interested party	Interested Party by his service as the Company's President and CEO	No	No
Education	BA in Economics (Tel Aviv University) MA in Business Administration (Tel Aviv University)	BA in Economics and Business Administration (Haifa University) MA in Economics (Technion)	B.Sc. in Industrial Management (Technion)
Business experience over past five years	President and CEO of the Company	Executive Vice President and CFO of the Company	Executive Vice President Global Supply Chain and Operations

Name of officeholder	Tali Mirsky-Lachman	Guy Gill	Yoav Barak
Position in corporation, subsidiary, related company or interested party	Global Vice President, Legal Affairs and Corporate Secretary	Vice President Finance. Serves as director in Frutarom subsidiaries.	Internal Auditor
ID no.	029423837	24223380	53670352
DOB	1972	1969	1955
Year began serving in the company	2010	2006	2004
Independent authorized signatory	No	No	No
Interested party in the corporation or relative of senior officeholder or of interested party	No	No	No
Education	L.L.B in Law and Business Administration (IDC, Herzliya)	BA in Economics and Accounting (Haifa University)	BA in Economics and Accounting (Haifa University)
Business experience over past five years	VP General Counsel and Corporate Secretary at Alvarion Ltd. until 2010	VP Finance of the Company	Has served as Internal auditor for corporations and as chairman and a director in various companies.

Regulation 26B – Independent Signatories

The Company does not have independent signatories as the term is defined under clause 37(d) of the Securities Regulations, 1968.

Regulation 27 – Company Auditors

The Group's external auditors are Kesselman & Kesselman, 1 Nathanson St., Haifa 3303473, Israel.

To the best of the Group's knowledge the auditors are not interested parties and/or related to any senior officeholder or interested party in the Group.

Regulation 28 – Changes to Memorandum or Articles of Association

No changes were made in the Company's Memorandum or Articles in 2014.

Regulation 29 – Recommendations and Resolutions by the Directors and by the Special General Meeting of Shareholders

Recommendations of the Board of Directors to the General Meeting of Shareholders and its decisions that do not require the approval of the General Meeting of Shareholders:

a) On March 18, 2014 the Company's Board of Directors resolved on the distribution of a dividend of NIS 0.28 per share, totaling NIS 16,382 thousand.

b) After the balance sheet date, on March 15, 2015 the Company's Board of Directors resolved on the distribution of a dividend of NIS 0.38 per share, totaling NIS 22,291 thousand.

Resolutions of the Extraordinary General Meeting:

c) On January 14, 2014, the Company's general meeting of shareholders resolved:

- To re-appoint Messrs. Yaacov Elinav and Isaac Angel as external directors in the Company for an additional period of three years, beginning on their date of appointment by the Meeting, under the terms of engagement in place up until the date of this meeting, and to appoint Ms. Dafna Sharir as an external director in the Company for a period of three years, beginning on her date of appointment by the Meeting, under the existing terms of directors' engagement at the Company.

- To approve the Company's Compensation Policy. For details of the Compensation Policy approved, see the Company's report on the matter dated December 29, 2013.
- To approve the purchase of an insurance policy for directors and officeholders who are not the principal shareholder or related to him, as detailed in Regulation 22 (c) above.

For more details, including the full wording of the General Meeting's resolutions, see the reports on the General Meeting dated December 29, 2013 and January 14, 2014.

<u>Regulation 29A – Company Resolutions</u>

In this matter, see Regulation 22 above (transactions with controlling shareholders), the resolution of the Board of Directors under Regulation 29 (c) above, and the Company's reports regarding the general meetings of December 29, 2013 and January 14, 2014.

Date: March 15, 2015

Frutarom Industries Ltd.

By:	______________________	______________________
Name:	Dr. John Farber	Ori Yehudai
Office:	Chairman of the Board	President and Chief Executive Officer

SECTION E

Report on the Effectiveness of the Internal Controls on the Financial Reporting and Disclosure

Annual Report on the Effectiveness of the Internal Controls on the Financial Reporting and Disclosure

The management of Frutarom Industries Ltd (the "**Corporation**"**)**, supervised by the Corporation's Board of Directors, is responsible for prescribing and conducting proper internal control on the Corporation's financial reporting and disclosure.

For this matter, the members of management are:

1. Ori Yehudai, President and CEO
2. Alon Granot, Executive Vice President and CFO
3. Amos Anatot, Executive Vice President Global Supply Chain and Operations.
4. Sharon Ganot, Global Vice President, Human Resources
5. Guy Gill, Vice President Finance
6. Tali Mirsky-Lachman, Global Vice President, Legal Affairs and Corporate Secretary
7. Yossi Cohen, Global Chief Information Officer

Internal control on financial reporting and disclosure includes controls and procedures which are conducted in the Corporation, which are planned by the President and CEO and the CFO and under their supervision, or by whoever fills these positions in practice, under the supervision of the Corporation's Board of Directors. These controls and procedures are meant to provide a reasonable level of certainty regarding the reliability of the financial reporting and the preparation of the financial reports in accordance with the provision of the law, ensuring that the information the Corporation is required to disclose in the reports it publishes under the provisions of the law is gathered, processed, summarized and reported on the date and the manner prescribed by law.

Internal control includes, among other things, controls and procedures designed to ensure that the information the Corporation, as stated, is required to disclose is gathered and delivered to the Corporation management including to the President and CEO, and to the highest ranking financial officer to whoever fills these positions in practice, in order to allow timely decision making with regards to the disclosure requirement.

Due to its structural limitations, internal control on financial reporting and disclosure is not designed to provide absolute certainty that misrepresentation or omission of information in the reports will be avoided or revealed.

Management, supervised by the Board of Directors, tested and assessed the internal auditing of the financial reports and the Corporation's disclosure and its effectiveness. The assessment of the effectiveness of the internal control on financial reporting and on disclosure performed by management, supervised by the Board of Directors, included:

Mapping out and identification of the business processes which management deems very material to the financial reports and disclosure. Testing key controls and testing the effectiveness of the controls. Components of the internal control included control of closing processes for accounting periods, preparation and editing of financial reports and disclosures, controls on the level of the organization, general controls on information systems and controls on business processes: (1) sales and customers (2) material consumption, inventory and procurement.

Based on the assessment of effectiveness performed by management, supervised by the Board of Directors as explained above, and subject to the statements below regarding the acquired company (as defined below), the Board of Directors and Corporation management have concluded that the internal audit on the Corporation's financial reporting and disclosure as at December 31, 2014 is effective.

Manager's Declarations

Declaration of the President and CEO

The undersigned, Mr. Ori Yehudai, hereby declares as follows:

1. I have reviewed the Periodic Report of Frutarom Industries Ltd. (the "**Corporation**") for 2014 (the "**Reports**");
2. To my knowledge, the Reports do not include any false representations of any material fact and do not omit representation of any material fact required in order to ensure that the representations contained in these, in light of the circumstances under which they were included, are not misleading in relation to the period of the Reports;
3. To my knowledge, the financial reports and other financial information contained in the reports duly reflect the Corporation's financial situation, its results of operations and cash flow for the dates and periods to which the Reports relate in all material aspects;
4. I have disclosed to the Corporation's auditors, the Board of Directors and the Audit Committee of the Corporation's Board of Directors, based on my most updated assessment of the internal control on financial reporting and disclosure:
   a. All the material deficiencies and weaknesses in prescribing and implementing the internal control on the financial reporting and on the disclosure, if any, which may reasonably adversely affect the ability of the Corporation to gather, process or report on financial information in a manner which could raise concerns regarding the reliability of the financial reporting and the preparation of the financial reports in accordance to the provisions of the law; and –
   b. Any fraud, material or not material, which involves the CEO or anyone directly reporting to him or other employees who hold significant positions in the internal control on the financial reporting and on disclosure;
5. I, alone, or together with others in the Company:
   a. Set controls and procedures, or ensured the existence and set up of controls and procedures under my supervision, designated to ensure that

material information relating to the Corporation, including its consolidated companies as defined in the Securities Regulations (Compiling Annual Financial Reports), 5770-2010, is brought to my attention by others in the Corporation and the consolidated companies, particularly during the preparation of the Reports; and

b. I set controls and procedures, or ensured the enactment and performance of controls and procedures under my supervision, designed reasonably ensure the reliability of the financial reporting and the preparation of the financial reports in accordance with the provisions of law, including in accordance with accepted accounting principles:

c. I have assessed the effectiveness of the internal control on the Corporation's financial report and on the disclosure, and presented the conclusions of the Board of Directors and of the management regarding said effectiveness of the internal control in this report as of the date of the reports.

The above does not derogate from my lawful responsibility, or from the lawful responsibility of any other person.

Date: March 15, 2015

____

Ori Yehudai
President and CEO

Manager's Declarations

Declaration of the Executive Vice President and CFO

The undersigned, Alon Granot, hereby declares as follows:

1. I have reviewed the financial reports and other financial information contained in the reports of Frutarom Industries Ltd. (the "**Corporation**") for 2014 (the "**Reports**");

2. To my knowledge, the financial reports and other financial information contained in the Reports do not include any false representations of any material fact and do not omit representation of any material fact required in order to ensure that the representations contained in these, in light of the circumstances under which such representations were included, are not misleading in relation to the period of the Reports;

3. To my knowledge, the financial reports and other financial information contained in the reports duly reflect the Corporation's financial situation, its results of operations and cash flow for the dates and periods to which the Reports relate in all material aspects;

4. I have disclosed to the Corporation's auditors, the Board of Directors and the Audit Committee of the Company's Board of Directors, based on my most updated assessment of the internal control on financial reporting and disclosure:

    a. All the material deficiencies and weaknesses in prescribing and implementing the internal control on the financial reporting and on the disclosure, if any, which may reasonably adversely affect the ability of the Corporation to gather, process or report on financial information in a manner which could raise concerns regarding the reliability of the financial reporting and the preparation of the financial reports in accordance to the provisions of the law; and –

    b. Any fraud, material or not material, which involves the president and CEO or anyone directly reporting to him or other employees who hold significant positions in the internal control on the financial reporting and on disclosure;

5. I, alone, or together with others in the Corporation:

   a. Set controls and procedures, or ensured the existence and set up of controls and procedures under my supervision, designated to ensure that material information relating to the Corporation, including its consolidated companies as defined in the Securities Regulations (Compiling Annual Financial Reports), 5770-2010, as may be relevant to the financial reports and other financial information contained in the Reports, is brought to my attention by others in the Corporationand the consolidated companies, particularly during the preparation of the Reports; and

   b. Set controls and procedures, or ensured the enactment and performance of controls and procedures under my supervision, designed reasonably ensure the reliability of the financial reporting and the preparation of the financial reports in accordance with the provisions of law, including in accordance with accepted accounting principles;

   c. I have assessed the effectiveness of the internal control on the Corporation's financial report and on the disclosure, insofar as such relate to the financial reports and to any other financial information contained in the reports as of the date of the reports; my conclusions regarding my aforesaid assessment has been brought before the Board of Directors and the management and is contained in this report. .

The above does not derogate from my lawful responsibility, or from the lawful responsibility of any other person.

Date: March 15, 2015

____

Alon Granot
Executive Vice President and CFO