Annual Report 2013

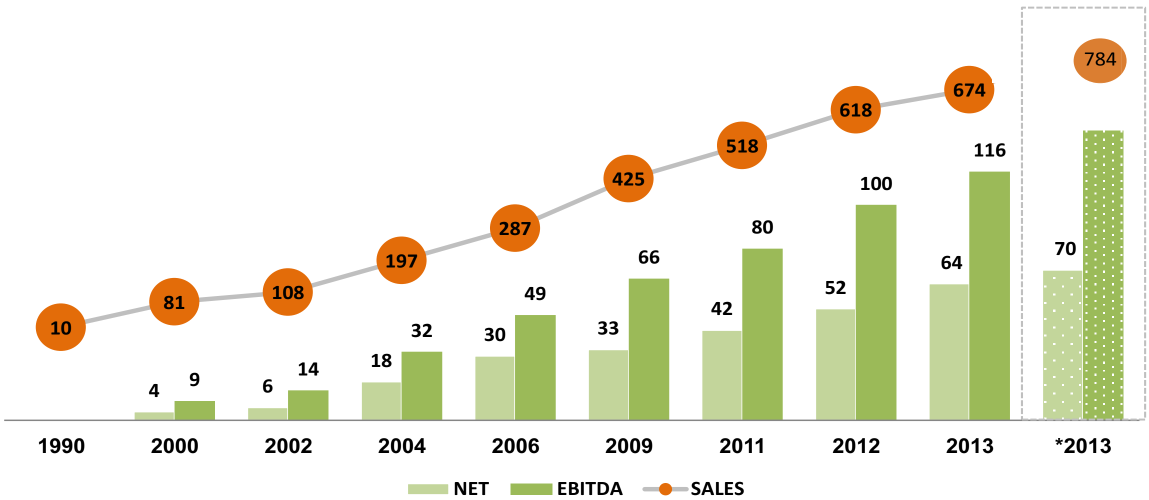
To Be The Prefered Partner For Tasty And Healthy Success

FRUTAROM
FOUNDED 1933

Dear Shareholder,

We are pleased to share with you the results of another record year – a year in which we achieved a further quantum leap in Frutarom's positioning and results. The successful implementation of our strategy combining profitable organic growth with the execution of strategic acquisitions has led Frutarom to achieve an average annual growth of 18% since 2000, supported by strong organic growth and successful integration of 30 acquisitions. Frutarom revenues and profits over this period increased from $81 million of revenues and an EBITDA of $9 million, to record high revenues of $674 million and $116 million of EBITDA. Net profit in 2013 has reached $64 million and cash flow generated from operating activities is $88 million.

In 2013 Frutarom revenues would have reached $784 million and net profit would have been $70 million, if the four acquisitions made in 2013 had been consolidated on 1.1.2013.

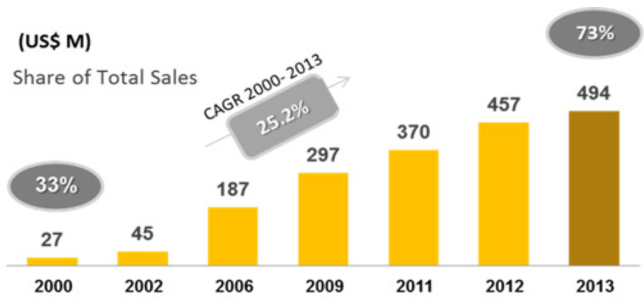


*2013- revenues and net profit combined with the four acquisitions made in 2013, had they been acquired and consolidated on 1.1.2013

In parallel to achieving profitable growth in our activities, we have focused, over the last few years, on the following four major business areas:

A. Strategically changing the product mix while significantly increasing our Flavors activity, the most profitable of our activities, and improving the product mix of our Specialty Fine Ingredients activity;
B. Changing the geographic sales mix, significantly increasing the share of revenues from developing countries and the United States;
C. Improving margins and profit through optimal utilization of our resources, as these change with the acquisitions, while creating operational savings and strengthening our competitive advantage;
D. Continue strengthening our position as a significant player in the global flavor and fine ingredients market, strategically positioned at the crossroad between the growing worlds of taste and health.

The results we have achieved speak for themselves, and reflect the successful implementation of our strategy while achieving the goals we have set.

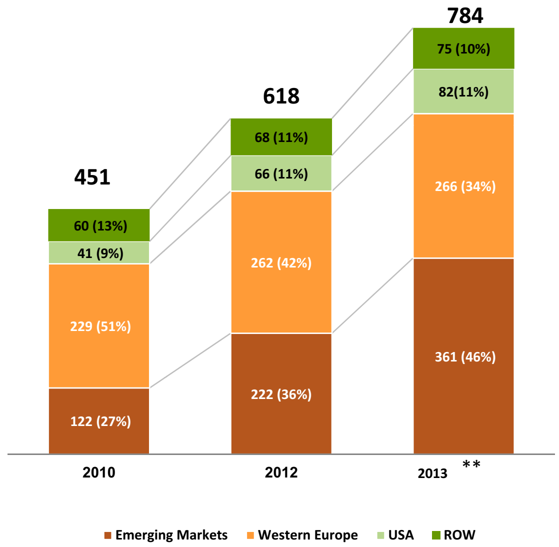


The implementation of our strategy to **significantly increase the share of our Flavors activity,** the most profitable of our activities, has led to an increase of the share of the Flavors activity to 73% of total sales, compared with 33% of in 2000, achieving a growth rate that is higher than that of the markets in which we operate.

Over the last few years we managed to improve our product mix in the Specialty Fine Ingredients activity. Frutarom's R&D labs have successfully developed new and innovative specialty natural ingredients, targeted for both the flavors and the health markets. Successful penetration of these products has contributed – and will continue to contribute – to an increase in revenues of our Specialty Fine Ingredients activity as well as improvement in margins.

Frutarom's accelerated expansion into emerging markets where growth rates are high was achieved with the support of organic profitable growth and strategic acquisitions.

Sales according to geographic regions 2010 - 2013



** 2013 sales combined with the four acquisitions made in 2013, had they been acquired 1.1.2013

Over the last three years we have tripled our revenues in the emerging markets and the share of the revenues from these markets has increased from 27% of sales in 2010 to 46% this year** The acquisition of JannDeRee in South Africa, PTI in Russia, Aroma in Guatemala and Hagelin in the USA (which has sales in Africa and in Latin America),

Significant increase in our activities in the United States

Over the last three years, revenues in the United States have doubled. At the same time, the Flavors activity in the United States, which is an area of focus, grew by a factor of four**.

As a result of the increase in the share of revenues from emerging markets and in the United States, the share of our revenues from Western Europe is now 34%**, compared with 51% in 2010.

<u>Frutarom acquisitions in 2013 and beginning of 2014:</u>

JannDeRee South Africa	PTI Russia & CIS	Aroma Guatemala	Hagelin USA	CitraSource USA
• Strengthening market position in **South Africa and Africa**. • Complementary Savory activity	• **Strengthening** Leadership in **East Europe** • Savory Solutions leadership	• Strengthening market position in **Central America.**	• Strengthening market position **in the US & EM** • Expertise in **beverages**	• Strengthening **Citrus** capabilities and leadership • Presence in **Florida** – world center for citrus

The trend of improved profit and gross and operating margins continued in 2013.

The Operating margin of Frutarom's core activities (Flavors and Specialty Fine Ingredients), net of one-time expenses for reorganization and acquisitions, increased by 24.1%, reaching a record high of $91 million with an operating margin of 14.3% of sales, the EBITDA increased by 18.4%, reaching a record high of $119.5 million with an EBITDA margin of 18.8%.

Net profit and earnings per share (net of one-time expenses) increased by 28.3% and 27.0% respectively, reaching $67.5 million and $1.16 compared with $52.6 million and $0.91 in 2012. Net margin reached 10.0% compared with 8.5% in 2012.

The growth in profits and improvement in profitability resulted from organic growth in sales, improved product mix in the core business, stability in the prices of the raw materials we use for our products and the successfully integration of the acquisitions made into our global activity, according to plan. We continue to work towards leveraging the many cross-selling opportunities presented by the acquisitions, taking full advantage of the many technological capacities we have gained and realizing savings resulting from consolidation of the R&D, sales, marketing, supply chain, operating and purchase infrastructures.

We successfully implemented the planned projects to streamline and optimize our resources following the acquisitions, and we aim to achieve our goal of realizing significant savings in the range of $10 million. These projects have started bearing fruit in the second half of 2013. The integration of the acquisitions made in 2013 and the one made in 2014, already started and expected to contribute to the growth in revenues profit and improvement in margins in 2014 and beyond. Following these last acquisitions, more opportunities for extracting operational efficiencies have opened up, and we are already working on plans to realize them.

We continue to build and strengthen our global purchasing system, leveraging the significant buying power that Frutarom now has following the acquisitions, and expanding our supplier network with an emphasis on purchasing of raw materials used in our products, at source.

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 taste and health. We witness the continued rapid shift that food and beverage companies have made following consumer demand, to the use of natural raw materials and flavors, with an emphasis on low-fat, low-sodium, low-cholesterol foods bearing the Clean Label, which are considered more nutritious, healthier and more environmentally friendly. Frutarom, with about 2/3 of its products being natural, has uniquely positioned itself as the provider of solutions combining flavor and health, made for the most part from natural products using new and innovative products based on cutting-edge technologies, realizing Frutarom's vision:

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

We intend to continue and expand our business with the large multinational customers, offering them unique innovative products, as well as with medium sized and domestic customers, with the focus to provide them services customized for their unique needs, including technological and marketing support, assistance in development of products and a high quality of service and tailor-made solutions, at the same level as usually provided to large multinational companies. In particular, we are focusing on increasing our market share among the private label customers (growing at a higher rate than the branded food industry), that are currently one-third of our Flavors' customer portfolio.

Frutarom today is a one of the leading global players in the industry, with an extensive product range, wide geographic spread and a diversified and excellent customers' portfolio. We have succeeded in achieving the ambitious goals we have set for ourselves and have made a quantum leap in our activities. The continued successful implementation of our strategy, the penetration into emerging markets where growth rates are higher than the global average, and into the United States, the consolidation and optimization of our operational resources and purchasing systems, the successful integration of the acquisitions made combined with successful execution of future ones that are in the pipeline, supported by our strong capital structure, will lead us to a further leap in revenues, profit and margins.

We believe that a revenue target of one billion dollars, and an EBITDA margin of 20% in our core business (Flavors and Specialty Fine Ingredients), will serve as a further catalyst for the continued strengthening of Frutarom's position, while creating value to our shareholders.

We are certain that with the cooperation of our devoted employees, led by our global management team and with the ongoing support of the members of the Board of Directors and yours, our shareholders, we will be able to continue expanding and successfully withstand the challenges that stand before us and achieve our ambitious goals.

Sincerely Yours,

Dr. John Farber
Chairman of the Board of Directors

Ori Yehudai
President and CEO

March 18, 2014

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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 fact that they use 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, based, among other things, on the information available to it 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, the effect of global economics; competition in the markets in which the Group operates; changes in demand for the Group's products; the Group's failure to successfully identify future acquisitions and acquire additional companies and activities; the impact of laws, regulations and standards, especially in the areas of environmental protection, health and safety; currency fluctuations; fluctuation in the prices of raw materials used by the Group and its ability to acquire these.

CHAPTER A

DESCRIPTION OF THE COMPANY'S BUSINESS

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The following terms will have the meaning ascribed to them:

“Aroma”	The Guatemalan Aroma Group
“Aromco”	Aromco Ltd.
"CH Italy"	Christian Hansen ITALIA S.p/a
“CitraSource”	The business activity and assets of the CitraSource LLC. Company and 100% of the issued share capital of CitraSource LLC Holdings of Florida, USA
“Director’s Report”	Report of the Board of Directors of the Company as at Dec. 31, 2013, 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, 2012, attached as Chapter 3 to this report
"Flavor Systems"	
"GDRs"	Flavor Systems International Inc.
"Gewurzmuller "	Global Depositary Receipts
Hagelin	Gewurzmuller GmbH and Blessing Biotech GmbH
	Hagelin & Company Inc. LLC and BRC Operating Company
JannDeRee	JannDeRee(Pty)
"Mylner"	Mylner Indústria E Comércio Ltda and its mother company, Vila Osório Participações s/a
"Oxford"	Oxford Chemical Limited
“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 "Financial Statements"	The Company's financial statements as at December 31, 2013, attached as Chapter 3 to this report
The "Group" or "Frutarom"	Frutarom Industries Limited, including its affiliated 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

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

CHAPTER 1 – THE COMPANY'S BUSINESS AND 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 company under the name Frutarom NewCo (1995) Ltd. In 1996 the Company's shares were listed for trade on the Tel Aviv Stock Exchange, and the Company changed its name to Frutarom Industries Ltd.

1.2. Frutarom Ltd., a wholly owned subsidiary of the Company through which the Company operates and manages its business and production activity, 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 fine ingredients materials and essential oils.

1.3. In February 2005 the Company raised capital from international and Israeli institutional investors by issuing shares and registering GDRs for trade on the London Stock Exchange Official List

1.4. Today, Frutarom is a global company, one of the ten leading companies in the world in the fields of flavors and specialty fine ingredients. Frutarom is engaged in the development, production and marketing of flavors and specialty fine ingredients used in the production of food, beverages, flavor, fragrance, pharmaceutical/nutraceutical, cosmetics and personal care products and other products. Frutarom operates 33 production facilities, 38 research labs and 69 sales and marketing centers in Europe, North America, Latin America, Israel and Asia that serve a customer base of over 15,500 in more than 145 countries. The Company markets and sells over 31,000 products and employs roughly 2,700 people throughout the world.

1.5. Frutarom has adopted a strategy which combines rapid and profitable organic growth with acquisitions and leveraging the synergies which these bring. Over the past few years Frutarom has focused on the following strategic goals:

- **Increasing the geographic spread** of its activities while accelerating growth and increasing its market share also in **emerging markets,** where growth rates are higher than market average, including in China, South and East Asia, Central and South America, Central and Eastern Europe and Africa, and in **North America**, in order to maximize the potential and the many business opportunities that exist in these fast growing markets.

- **Combining flavor and health** –Frutarom develops innovative flavor 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 give the Company an important competitive advantage among customers in both developed and emerging markets. These new and innovative products are for the main part of higher margins, and therefore contribute not only to growth in sales but also to Frutarom's improved product mix and profitability.

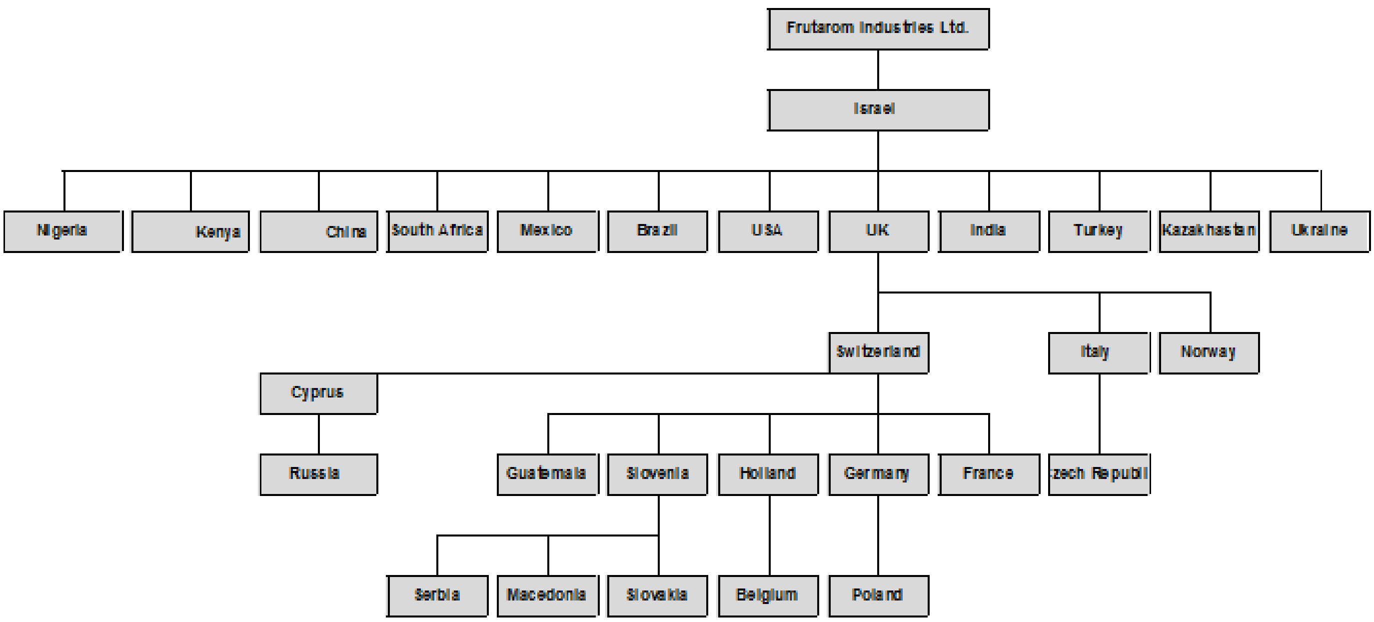
- **Focusing on medium-/ small- size customers and private label customers, who together make up a considerable portion (over 60%) of the food manufacturing market, and sale of specialty solutions to multinational food manufacturers -** Frutarom continues to expand the services it provides its customers and its product portfolio and solutions, for both large multi nationals and for medium-sized and domestic companies, with a special emphasis on the fast growing private label market. In the large multinational food and beverage market sector, Frutarom will continue to focus on specialty products and expansion of its natural product portfolio. In the medium-sized and domestic market sector, Frutarom offers the same high level of service and tailor made solutions as are usually provided for the large multinationals. Frutarom also offers its medium-sized and domestic customers and private label customers, who are usually of more limited resources compared to the large multinationals, assistance in the development of their products, providing marketing support and flexibility with regard to minimum quantities and dates of delivery

- **Acquisitions and mergers and their contribution to 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 in order to leverage the many cross-selling and operational savings opportunities and to 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 has continued implementing 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, and in the beginning of 2014 made the further acquisition of the American CitraSource.

For further information on the Company's growth strategy see section 40 of this report.

1.6. The Company's main shareholder is the ICC Group which, through ICC Industries Inc.[1], holds 21,358,034 shares as of the date of this report, 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] ICC Industries Inc., through its subsidiaries, holds the abovementioned shares. In addition to these shares, 488,888 shares (approx. 0.08% of the Company's issued and paid up share capital) are held directly by Dr. John J. Farber, who also serves as the chairman of the Company's board of directors and his wife, Mrs. Maya Farber, who serves as directors in the Company, and are the controlling members of ICC Industries Inc. Their daughter, Ms. Sandra Farber, also serves as a director in the Company.
[2] The structure of the Group is presented according to countries. Except for Frutarom's subsidiary in South Africa, Russia, China, Turkey and Ukraine, Frutarom holds 100% of the share capital of the Groups' main companies. For further details regarding Frutarom's subsidiaries, see Note 23 to the Financial Statements.

1.7. During the second half of the 1980s, with the change of Frutarom's management, a new business strategy was adopted which promoting material growth in the Company's international activities allowing Frutarom to become a global company and a leader in its field by substantially expanding the Company's Flavor activity, the Company's most profitable field of activity.

In the early 1990s, Frutarom's management decided to expand its global activity through the acquisition of companies and activities in the Company's fields of activity.

Since 2001, Frutarom has accelerated its growth rate 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. Frutarom has significantly increased its mergers and acquisitions activity over these years, and executed 30 acquisitions to date.

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

1.8.1. **Acquisition of EAFI's activity and assets** - on January 20, 2011 Frutarom signed an agreement for the acquisition of the activity and assets of the UK company EAFI in consideration for US$4.8 million (GBP 3 million). The acquisition was completed on January 31, 2011.

EAFI, founded in 1979, develops, manufactures and markets savory solutions including flavors, seasoning mixes and functional ingredients to the food industry in general, and to the processed convenience food, snacks and processed meat and fish industries in particular. EAFI has a wide customer base and a development, manufacturing and marketing site in the UK.

EAFI's activity is highly synergetic with that of Frutarom in the UK as well as with Frutarom's savory activity in Europe, which increased substantially in recent years.

For further information regarding the acquisition of EAFI, see the Company's immediate reports in the matter dated January 23, 2011 and February 1, 2011 and note 5.b to the financial statements.

1.8.2. **Acquisition of Savory assets and activities of CH Italy -** on May 26, 2011 Frutarom signed an agreement to acquire the assets and savory activity of Christian Hansen Italia in return for €25 million. The acquisition was completed on July 29, 2011.

CH Italy's savory activity develops, produces and markets unique and innovative savory solutions including flavors, seasoning compounds and functional ingredients for the food industry, with special emphasis on processed meat and convenience food applications. The acquired activity is a leader in savory solutions with an extensive customer base comprised mainly of the leading Italian meat processors; the activity also has sales force in Russia, Ukraine, Poland, Czech Republic and France. The activity also included a state-of-the-art, high-capacity plant located in Parma, Italy that enables Frutarom to increase its activities and to take advantage of operational synergies with its existing savory activities in Europe, and innovative R&D laboratories.

For further information regarding the acquisition of CH Italy, see the Company's immediate reports published on May 26, 2011, July 31, 2011 and November 23, 2011 and note 5.c to the Financial Statements.

1.8.3. **Acquisition of Aromco -** on August 19, 2011 Frutarom signed an agreement to acquire 100% of the share capital of the UK company **Aromco** Ltd. for approximately US$24.6 million (GBP15 million). The acquisition was completed upon signing.

Aromco, founded in 1985, develops, manufactures, and markets flavors for the food and beverage industry. Aromco is mostly active in emerging markets with high growth potential in Eastern Europe, Africa and Asia as well as in the UK. Aromco operates a plant in Hertfordshire, England. Aromco's activities are greatly synergetic with Frutarom's activities in the UK, and with Frutarom's Flavor activities.

For further information regarding the acquisition of Aromco, see the Company's immediate reports published on August 21, 2011 and December 1, 2011 and note 5.d to the Financial Statements.

1.8.4. **Acquisition of Flavor Systems -** on September 13, 2011 Frutarom signed an agreement to acquire 100% of the shares capital of Flavor Systems in return for the sum of US$45.3 million, (not including the future earn out payment as noted below). In addition, Frutarom paid US$6.5 million for real-estate assets owned by other companies held by the shareholders of Flavor Systems. The acquisition was completed on October 3, 2011. In December 2012 the Company paid an additional amount of US$10 million, according to the future earn out mechanism included in the acquisition agreement.

Flavor Systems, established in 1994, develops, manufactures, and markets sweet and savory flavors for the food and beverages industry. Flavor Systems owns a modern plant and R&D laboratories located in Cincinnati, in the Mid-West of the USA. The acquisition also included a new and advanced production site with a high production capacity. The site has allowed substantial expansion in areas, among others, where Frutarom has not yet operated until now in the US, such as flavored coffee and shakes sold in convenience stores and in leading food chains throughout the US. Through this acquisition, Frutarom also entered the field of savory flavors, where it did not [yet] operate in the US prior to the acquisition. Frutarom has acted to utilize operational synergies between Flavor System and its flavors activity in North America, among other things by integrating sites and activities. Frutarom's flavor activity has been transferred from its plant in New Jersey to the new and advanced plant in Cincinnati, which serves as Frutarom's new flavors center in North America.

For further information regarding the acquisition of Flavor Systems, see the Company's immediate reports published on September 13, 2011, October 4, 2011 and December 25, 2011 and note 5.e to the Financial Statements.

1.8.5. **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 approximately US$5.8 million (GBP3.8 million), and additional payment of US$430 thousand (£268 thousand), calculated based on performance, in accordance with a mechanism prescribed in the purchase 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, 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 manufacturers and private labels in the UK and in emerging markets.

Savoury Flavour's production site is located near the production site the Company acquired from EAFI, as described in section 1.7.1 above, also a savory production site. The geographic proximity between the sites, the complementary product portfolio and technologies of the two activities have enabled shared management of the two sites and integration of activities, creating significant synergies between the two activities and with Frutarom's growing savory activity in the UK and throughout the world, which have significantly increased over the past few years.

For further information regarding the acquisition of Savoury Flavours, see the Company's immediate report published on January 5, 2012 and note 5.f to the Financial Statements.

1.8.6. **Acquisition of Etol -** over the first half of 2012, Frutarom purchased the entire share capital of the Slovenian public company ETOL for an overall sum of €35.4 million.

Etol, founded in 1924, develops, manufactures, and markets sweet and savory taste solutions, focusing on natural flavor products for the food and beverage industry. Etol also has great experience in the development and manufacture of fruit based flavors and products and food systems, specializing in local fruits of the region, as well as extensive activities in the growing area of bases for beverages, in which Frutarom invests and expands its activities. Etol products are sold to a wide customer base in Central and Eastern Europe and in emerging markets, with a focus on, Russia, Poland, Ukraine, Slovenia, Croatia, Serbia, Slovakia, Belarus, Macedonia, Czech Republic, Kazakhstan, Turkey and other developed countries including Switzerland, Germany and England. Etol's customers include leading food and beverage manufacturers in the countries it operates, including large multi-national food companies. Over the last year Frutarom has transferred some of its flavor activities in Israel and in Switzerland to the Etol site (and to the UK), thus creating 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.g to the Financial Statements.

1.8.7. **Acquisition of Mylner -** on February 7, 2012 Frutarom signed an agreement, to acquire 100% of the share capital of the Brazilian company Mylner in return for US$15.7 million (BRL27.1 million). Frutarom paid a further BRL4.4 million for Mylner's cash balance. The acquisition was completed upon signing.

Mylner, founded in 1974, develops, manufactures and markets flavor solutions, focusing mainly on 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. Mylner’s wide customer base includes leading food and beverage manufacturers mainly in Brazil and in other developing countries in Latin America.

For further information regarding the acquisition of Mylner, see the Company’s immediate reports published on February 7, 2012 and note 5.h to the Financial Statements.

1.8.8. **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 in consideration for US$5 million. The acquisition was completed upon execution.

JannDeRee, founded in 1993, develops, manufactures, and markets flavors with an emphasis on savory flavors and sweet flavor solutions. JannDeRee, which over the past few years has grown at a fast pace, has a development, production and marketing site in Johannesburg, South Africa, to which Frutarom activity in South Africa was transferred following the acquisition. JannDeRee also has and a wide customer base in South Africa and in other important emerging 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 rates higher than the rate of market growth over the past few years.

The integration of JannDeRee’s with Frutarom's activity in South Africa was completed over the third quarter of 2013, including integration of sites, of management and purchasing, production and supply chain systems, and integration of the research and development, marketing and sales systems.

For further information regarding the acquisition of JannDeRee, see the Company’s immediate report published on May 2, 2013 and note 5.i to the Financial Statements.

1.8.9. **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”), holder of the Russian PTI group in consideration 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 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. 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 raw materials for the food industry (including specialty protein based raw materials it manufactures using advanced technology), with a special focus on processed meat and convenience foods. PTI also has trade and marketing activity, offering its customers raw materials not manufactured by PTI as part of the services it offers its customers in providing comprehensive solutions.

Frutarom’s is acting to leverage of PTI’s R&D, marketing and sales infrastructure in Russia and in the markets in Central and Eastern Europe in which it operates, as well as Frutarom’s global distribution and sales infrastructure, in order to leverage and realize the many cross-selling opportunities this acquisition brings, by expanding the customer base and of Frutarom’s product portfolio. The integration of Frutarom’s activities with PTI’s in the countries in which the two companies operate will present additional synergies as well as achieving significant operational savings.

For further information regarding the acquisition of PTI, see the Company’s immediate reports published on November 18 and 20, 2013 and note 5.j to the Financial Statements.

1.8.10. **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 Panama company, holder of the Guatemalan Aroma group , in return for a net cash payment of US$12.5 million (US$13 million, with a deduction of Aroma’s cash balance and cash equivalents in the amount of US$0.5 million). The share purchase agreement contained a mechanism for payment of future consideration, under which an additional payment will be made at the rate of the EBITDA achieved above US$2.25 million over the years 2013 to 2015. 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 food. 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 Central America.

Aroma's sales turnover for the year ended on 31 December 2013 was US$6.2 million.

The acquisition of the Guatemalan Aroma joins the acquisition of the Brazilian Mylner completed by Frutarom at the beginning of 2012, and to Frutarom's independent operations in Costa Rica, which includes a development lab and sales and marketing infrastructure that is now integrated with Aroma activities. The acquisition will allow Frutarom to strengthen its position and presence in these important markets of Central and South America, while expanding its product portfolio and increasing its research and development, 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.k to the Financial Statements.

1.8.11. **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, produces and markets flavors and unique flavor technologies for the food industry, with a focus 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, and has a customer base including 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, markets with high growth rates.

Hagelin's sales turnover for the year ended on 31 December 2013 was US$23.6 million.

Hagelin's activity in the UK have already been integrated with Frutarom's activity in this country, and Frutarom is acting to integrate Hagelin's activity in the US and to utilize the many synergies in all the areas this acquisition offers.

For further information regarding the acquisition of Hagelin, see the Company's immediate report published on December 12, 2013 and note 5.I to the Financial Statements.

1.8.12. **Acquisition of CitraSource** - on February 24, 2014 Frutarom signed agreements for purchase of the American CitraSource, whose assets include, among others things, a plant for processing specialty citrus ingredients, intangible assets 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$7.5 million and also includes additional future payment based upon CitraSource's results for 2014-2018. The transaction was completed upon signing.

CitraSource, founded in 2003, specializes in research and development, production, marketing and sale of specialty solutions in citrus to leading global customers in the flavor and fragrance, food and beverage markets. CitraSource's customers include leading global flavors, food and beverage producers. CitraSource's knowhow, expertise and capabilities across all ranges of citrus (especially Orange, Grapefruit, Lemon, Lime and Tangerine), will help Frutarom expand its natural products portfolio. CitraSource also has global purchasing capabilities in citrus, and the combination of these with Frutarom's capacities is, in the opinion of the Company, expected to further strengthen Frutarom's position as a leading player in research, production and sales of citrus specialties, an essential ingredient for flavors and many food and beverages products.

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 its area of operations, which will contribute to Frutarom’s global purchase system. CitraSource's activities will be integrated into the Specialty Fine Ingredients division starting from the date of purchase, in the first quarter of 2014.

For further information regarding the acquisition of CitraSource, see the Company’s immediate report published on February 2, 2014 and note 22a to the Financial Statements.

1.9. The consolidation trend in the industry in which Frutarom operates is ongoing, Frutarom, which is one of the world's ten largest Flavors and Specialty Fine Ingredients companies [3], continues to be one of the leading and most active companies in acquisitions. Frutarom's management will continue to invest substantial resources in locating and pursuing potential new acquisitions which suit its strategy of rapid and profitable growth.

The Company estimates that its solid equity structure, the strong cash-flow achieved from its activities and the support from financial institutions will enable it to continue implementing its acquisitions strategy.

[3] Source: Leffingwell & Associates, October 2013

2. The Group's Fields of Operation

2.1 Frutarom is a global company that develops, manufactures, markets and sells flavors and specialty fine ingredients used in the production of food and beverage, flavors and fragrances, pharmaceutical/nutraceutical, cosmetics, personal care and other products. Frutarom has two main activities, each of which is a main field of activity and reported as a business segment in the Company's consolidated financial reports (see also Note 6 in the financial reports for 2013), considered by Company management to be Frutarom's **core business**:

2.1.1 **The Flavor activity** – As part of the Flavor activity, Frutarom develops, produces, markets and sells sweet and savory flavor solutions, including flavor essences and product containing, in addition to flavor essences, fruit, vegetable and other natural components (food systems), used mainly by manufacturers of food and beverages and other consumer products. Frutarom develops thousands of different flavors for its customers, most of which are tailor-made to the needs of specific customers. Frutarom also develops new formulas and adapts them to changing consumer preferences and customers' needs.

The Flavor Activity, Frutarom's grew in a rapid and profitable manner, and combined with organic growth and acquisitions, it now constitutes 73% of Frutarom's total sales (compared with 33% in 2000).

This accelerated growth is the result of (a) a focus on the fast growing area of natural flavors; (b) the development of innovation-based unique solutions combining taste and health for the large multi-national market sector; (c) focus on mid-size and local customers (in emerging and developed markets), focusing in particular on the growing segment of private label manufacturers, providing them with customized services, including technological and marketing support, product development support, tailor-made solutions, and high quality of services, as are normally provided to large multi-national companies; and (d) the result of Frutarom's strategic acquisitions, which have and are being successfully integrated with Frutarom's global activities.

2.1.2 **The Specialty Fine Ingredients activity** – As part of the Specialty Fine Ingredients activity, Frutarom develops, produces, markets and sells natural flavor extracts, natural functional food ingredients, natural pharmaceutical/nutraceutical extracts, natural biotechnology based algae products, aroma chemicals, essential oils, specialty citrus products, and natural gums. These unique specialty fine ingredients are sold principally to the food and beverage, flavor and fragrance, pharmaceutical/nutraceutical, cosmetics and personal care industries.

Frutarom's Specialty Fine Ingredients activity focuses on high value added product portfolio, giving it an advantage over its competitors. The majority of the specialty fine ingredients in flavor and health are natural products, for which demand in the market has increased at a higher rate than that of products which are not natural. Over the last few years, Frutarom has been focused on expanding its portfolio of natural ingredients, putting a special emphasis on the area of natural, functional and health foods.

2.2 In addition to Frutarom's core business, the Company also trades and markets various raw materials produced by third parties, as part of its service to its customers in the provision of comprehensive solutions. This trade and marketing activity is synergetic and supportive of Frutarom's core business as it leverages the sales, supply chain, purchase and global management system, and allows Frutarom to offer a wider variety of products and added value solutions to its customers, mainly medium size and domestic customers, and to strengthen the partnership with these customers. This activity, which grew following the acquisition of ETOL and PTI, focuses mainly on Central and Eastern Europe and Israel. In 2013, sales in this trade and marketing totaled approximately US$39.7 (5.9% of total Frutarom sales).

2.3 Frutarom's growth strategy is based on identifying major trends in the food and beverage markets and adjusting its activity accordingly, providing its customers solutions that address the forecasted needs of consumers. In recent years, an accelerated trend of a shift to the use of natural flavors and ingredients by food and beverage companies has been noted, with a special focus on functional foods (foods containing value-added nutritional ingredients) and on low-fat, low - sodium and low-sugar products and clean-label products perceived as having more nourishing, healthier and environmentally friendly qualities. Consumers demand healthier products without compromising the highest taste standards, despite the fact that many health ingredients also result in an aftertaste. Another trend arising in recent years is the number of hours the average consumer spends outside the home, resulting in increased demand for convenience food that is both tasty and healthy. This trend is supported by the rise in the scope of surplus consumer income and the willingness to increase spending on convenience products and other products perceived as healthier. In developed markets, we witness a continued trend of consumer demand for more natural and healthy food. Frutarom has identified these trends and uniquely positioned itself as a solution supplier combining taste and health in response to consumer needs. Maximizing the synergy between its various activities enables Frutarom to offer its customers excellent science-based taste solutions and value-added health qualities with a special focus 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 combination of innovative, natural products.

3. Investments in the Company's Capital and Transactions in its Shares

3.1 To the best of the Company's knowledge, no material investments were made in the company's capital and/or material transactions made during the years 2012- 2013 in the Company's shares outside the stock exchange 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 plan for Company employees, see Note 12b to the Company's Financial reports.

4. Distribution of Dividends

4.1 dividends to its shareholders as detailed in the following table:

Year	Dividend Per Share in NIS	Total Sum NIS ,000	Total Sum US$,000	Distribution Date
2012	0.20	11,565	3,029	May 6, 2012
2013	0.24	13,886	3,892	May 5, 2013

The stated dividend distributions did not require court approval.

4.2 As of December 31, 2013 the distributable retained earnings amount to US$371,373 thousand. Upon approval of the financial reports for the period ended December 31, 2013, the Board of Directors resolved to distribute a cash dividend in the amount of NIS 0.28 per share, an increase of 16.7% versus last year.

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

4.4 On February 16, 2012 the Company took upon itself a limitation on the distribution of a dividend, as part of the adjustment of its financial covenants, under which it is entitled to distribute:

(A) Up to 50% of the balance of surplus accumulated up to December 31, 2011, as this figure appears in the Company's balance sheet relating to 2011.

(B) Up to 50% of the Company's annual profits for each calendar year, as this figure will appear in the Company's financial statement for the calendar year in which these profits were 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 2013, Frutarom's sales grew by 9%, achieving a yearly high of US$674 million, compared with US$618 million in 2012. For further information regarding Frutarom's sales according to fields of activity, see section C to the Board of Directors' explanations to the state of the corporation's affairs in the Board of Directors' Report (Results of Activities in 2013).

5.2. The following tables show the Group's financial information for the years 2011 through 2013, broken down by fields of activity (in US$ 000):

2013 (in US$ 000)

		Area of activity		Adjustment to consolidated	Total core business	Trade & Marketing	Consolidated
		Flavors	Fine Ingredients				
Income	From externals	494,389	139,597	39,707	633,986	39,707	673,693
	From other fields of activity	-	5,994	(5,994)	5,994		-
Total Income		494,389	145,591	33,713	639,980	39,707	673,693
Expenses	Expenses that are income of other fields of activity	5,994	-	(5,994)	5,994	-	-
	Expenses that are not income of other fields of activity	418,776	129,212	38,941	547,995	38,791	586,929
Total Expenses		424,770	129,212	32,947	559,983	38,791	586,929
Operating Profit[4]		69,619	16,379	766	85,991	916	86,764
Profit attributed to non-controlling shares		232	618	-	850		850

[4] Total consolidated operating profit including operating profit attributed to non-controlling shares

2012 (in US$ 000)

		Area of activity		Adjustment to consolidated	Total core business	Trade & Marketing	Consolidated
		Flavors	Fine Ingredients				
Income	From externals	457,341	138,318		595,659	22,342	618,001
	From other fields of activity	-	2,445	(2,445)	-	-	-
Total Income		457,341	140,763	19,897	598,104	22,342	618,001
Expenses	Expenses that are income of other fields of activity	2,445	-	(2,445)	2,445	-	-
	Expenses that are not income of other fields of activity	395,419	128,385	21,349	523,804	21,342	545,153
Total Expenses		397,864	128,385	18,904	526,249	21,342	545,153
Operating Profit[5]		59,477	12,378	993	71,855	1,000	72,848
Profit attributed to non-controlling shares		-	621	-	621	-	621

2011 (in US$ 000)

		Area of activity		Adjustment to consolidated	Total core business	Trade & Marketing	Consolidated
		Flavors	Fine Ingredients				
Income	From externals	369,894	142,176	6,373	512,070	22,342	518,443
	From other fields of activity	—	2,832	(2,832)	2,832		—
Total Income		369,894	145,008	3,541	514,902	22,342	518,443
Expenses	Expenses that are income of other fields of activity	2,832	—	(2,832)	2,832	-	—
	Expenses that are not income of other fields of activity	320,251	133,263	6,265	6,265	21.342	459,779
Total Expenses		323,083	133,263	3,433	3,433	21.342	459,779
Operating Profit		46,811	11,745	108	108	1,000	58,664
Profit attributed to non-controlling shares		-	-	-	-	-	-

5 Total consolidated operating profit including operating profit attributed to non-controlling shares

5.3 Reasons for adjustment to consolidated – the intercompany sales, purchases and profit and loss are cancelled in the framework of the adjustment to the consolidated report.

5.4 Explanation of developments – For an explanation of developments that occurred in the data shown above, see the explanation in the Directors Report for the year ended December 31, 2013.

5.5 The allocation of the joint costs of the Flavor and Specialty Fine Ingredients activities is made on the site level where joint resources for both fields exist, based on relevant loading criteria for each of the joint resources. Any change to the loading criteria requires advanced approval of the Group's headquarters. In recent years there were no significant changes in the criteria for allocation of joint costs.

6. Market Environment and Influence of External Factors on the Company's Activity

Market Environment – Global Flavor and Fragrance Industry

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

6.1 The global flavors, aromas and raw materials market in 2012 was estimated at approximately US$23 billion[6]. Frutarom does not operate in the aroma essences market, but does operate in the markets for functional food ingredients (which is not included in the above estimation). Accordingly, the Company believes that the global market in which it operates is valued at approximately US$18.5 billion. Based on Leffingwell & Associates' data, Frutarom is ranked globally as one of the top ten companies in the field of flavors and fragrances.

6.2 In 2012 IAL Consultants[7] estimated that global sales in industrialized nations (the USA and Western Europe) in the flavors market would grow at an annual rate of 2% during the years 2012-2017. According to these estimations, the growth rate in emerging markets such as Asia, Central and South America, Eastern Europe and Africa is expected to be significantly higher as a result of changes in consumers' preferences in these markets and the shift to processed foods, and may reach an average annual rate of approximately 5.9% over the years 2012 – 2017.

6.3 The manufacturers acting in the flavors and fragrances and in the raw materials markets are divided into three main groups: 1. Large multinationals; 2. medium-size companies; 3. Domestic and small companies.

6 Leffingwell & Associates, October 2011, IAL Consultants October 2011
7 IAL Consultants April 2013

The large multinationals generally operate globally, and have sales turnovers in flavors of over a billion dollars. In the global flavors and fragrances market there are four such companies, which according to IAL Consultants represent about 60% of the market in sales terms. These multinationals focus mainly on customers which are large multinational food and beverage producers.

The domestic and small size companies have sales turnovers of less than US$100 million (most are much smaller, and sell in millions to several tens of millions). It is the Company's estimate that in the global flavors and fragrances market, there are some 500 such domestic and small companies, which according to IAL Consultants represent about 10% of the market in sales terms. These companies usually focus on customers which are small domestic food manufacturers having limited capacities in the area of research, development, innovation and tailor made service for customers.

Medium-size companies, among which Frutarom numbers, have flavors revenues between US$100 million and 1 billion. In the global flavors and fragrances market there are eight such companies, which according to IAL Consultants represent about 30% of the market in sales terms. Some of these medium-size companies are companies with a greater focus on a specific geographic region (such as the US, France, Japan) and some, such as Frutarom, are active in the global market.

6.4 The flavor and fine ingredients market in which the Company is active 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 and pharmaceutical/nutraceutical industries. In these industries, reliability, quality of service and the manufacturers' knowledge and understanding of the customers' needs is of great importance.
- Research and development – End user preferences are dynamic, creating a competitive customer market (usually in food or beverage). The market is characterized by an abundance of new and innovative products. Accordingly, manufacturers must invest heavily in research and development in order to offer a wide range of innovative products. Sometimes this investment is undertaken at the initiative of the flavor manufacturer while at other times it is the customers' initiative (food/beverage manufacturers) in collaboration with the flavor manufacturer.

- Compliance with quality and regulatory standards – Flavor and fine ingredients products are principally designated for the food and beverage and pharmaceutical/nutraceutical industries, which are subject to strict quality and regulatory standards. As a result, manufacturers are required to meet the same strict standards. In recent years quality and regulatory standards have become increasingly stringent, often intensifying the burden on competitiveness on small flavor manufacturers and increasing entry barriers for new players.
- The importance of flavors in the final product – Flavors play a major role in determining the taste of the end product and are often a vital element in determining success. Flavors cannot be precisely replicated and as they represent a relatively small percentage of the final product's overall cost, food and beverage manufacturers will usually avoid replacing the flavor and its manufacturer.
- Investment in production capabilities– In the fine ingredients field, considerable capital investment is required to build manufacturing facilities and/or increase existing production capabilities. These investments serve as a significant entry barrier for new manufacturers in the industry.

In light of the entry barriers described above, penetration of new manufacturers into the market is mainly through mergers and acquisitions. In general, the market is characterized by a trend of consolidation and a decrease in the number of players.

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

6.5 Frutarom is a global company that develops, manufactures, markets and sells flavors and specialty fine ingredients used in the production of food and beverage, flavors and fragrances, pharmaceutical/nutraceutical, cosmetics, personal care and other products. Frutarom operates principally in two activities, each of which constitutes a main field of activity - the Flavors activity and the Specialty Fine Ingredients activity. The Company considers these activities to be its core business.

6.6 In addition to its core activities, Frutarom also deals in import and export of a variety of raw materials as part of its service and comprehensive solutions it offers its customers. The trade and marketing activity is synergetic and supports Frutarom’s core activity as it leverages its sales and supply chain system, and its global purchasing and management systems allowing the Company to offer its customers, mainly the medium size and domestic customers, a wider variety of products, solutions and added value, and strengthen the partnership with them. This activity, which has grown as the result of the acquisitions of ETOL and PTI, focuses mainly on Central and Eastern Europe, and Israel.

6.7 The Company’s various activities are to a great extent complementary. This synergy may be observed in a number of areas:

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

- Research and development – The field personnel of the Flavor activity possess special knowhow and familiarity with the needs of food and beverage customers. This supports the development and production (benchmarking) of innovative specialty fine ingredients that meet customer needs.

- Operations – A number of Frutarom's production sites and its supply chain system are shared between the Frutarom’s various activities, thereby sharing resources.

- Fine ingredients – Most of the specialty fine ingredients produced by Frutarom are sold to third parties. Some of the fine ingredients are used by Frutarom's own Flavor Activity and some are produced solely for Frutarom, for the production of unique flavors that give Frutarom a unique competitive advantage in the market. The sale of raw materials as part of the Trade & Marketing activity also contributes, mainly in light of the advantage of size in purchase and its contribution to margin improvement.

In light of the considerable synergy that exists between the two activities and Frutarom's commitment to providing comprehensive solutions combining flavor solutions with specialty fine ingredients - some of which possess health qualities - and ingredients which are meant to aid in the creation of texture and richness of the food product, it is not always possible to separate the fields of activity.

Flavors Market

7. Overview of the Flavors Market

General

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

7.2 According to an estimate by IAL Consultants, an industrial and market research company[8], 2012 global sales of flavors for the industry amounted to approximately US$8.7 billion. Flavor products are sold primarily to producers of prepared food, beverages, dairy, bakery, processed meat and fish products, confectionery, oral hygiene, pharmaceutical products, animal feed and tobacco products

7.3 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. 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.

[8] IAL Consultants April 2013

7.4 The following table sets forth 2012 flavor sales by region and the projected annual growth rate in these geographic regions[9]:

Country	**Estimated world consumption in 2012 (US$ million)**	**Average growth expected in 2012-2017**
Western Europe	1,712	1.3%
Eastern Europe	585	2.7%
North America	2,470	2.4%
South America	651	7.6%
Asia	2,652	6.2%
Middle East and Africa	599	5.3%
Total	8,669	4.1%

7.5 According to the above projections, the largest market in flavors in 2012 was the Asian market, with 30.6% of the global market, and following this, the North American market, with 28.5%. From the point of view of estimated growth rates, the South American market is expected to grow at the highest rate (7.5%), followed by the Asian market with expected annual growth rates of 6.2% in the years 2012 – 2017. Frutarom has successfully increased its penetration into these growing markets in Asia, North and South America, Eastern Europe, the Middle East and Africa, and will continue to act for accelerated penetration into these markets. The Company also acts to deepen its business relations and maximize sales synergies in the Western European market. Frutarom acts to deepen its penetration into the global flavors market, among other things by focused strengthening of the research and development, which will lead to the development of new and innovative products in line with customer demands, by strengthening production, marketing and sales systems in important target countries, taking advantage of the synergies from acquisitions completed over the past few years and continuing exploration of options for additional strategic acquisitions.

<u>Characteristics of the Flavors Market</u>

7.6 Reliable, quality 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.

[9] IAL Consultants, April 2013.

As a result large multinational customers, and increasingly also mid-sized customers, have reduced the flavor suppliers that they will work with to a select few named on their "core lists", creating an entry barrier for small flavor manufacturers.

7.7 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 order to ensure a continuous stream of innovative products and to maintain profitability and growth for any flavor manufacturer. The initiative for the development of new flavor products can be spurred by the flavor manufacturer or by a customer in need of a specific flavor to be used 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 and benchmark the taste preferences of various end product types and target markets. In addition, as most flavors are tailor made for specific customers, a close collaborative relationship with the customer is essential, but customers are also less likely to change suppliers for such flavor products during the course of the end products' life cycle. These flavor formulas are commercial secrets and usually remain the property of the flavor manufacturer. As most flavor products are tailor made for specific customers, customers will usually refrain from changing suppliers for the lifetime duration of the final product.

7.8 Low price sensitivity – Since flavor products play a major role in determining the flavor of the end product, 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.

7.9 Production processes – Flavor products in general and flavor extracts in particular typically contain a variety of ingredients (typically dozens per flavor), which are blended using unique formulas created by a manufacturer's flavorists. 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.

7.10 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 ingredients industry.

7.11 Entry barriers – for explanations regarding entry barriers characterizing the flavor market, see section 6.4 above.

Characteristics of the Food and Beverage Market

7.12 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 US$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- and small sized food and beverage producers -size and local food and beverage producers will continue to play a significant role in the market.

7.13 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 these customers limited service, and do not invest much resources in the development of tailor-made flavors for their needs. 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 often do not have the product variety and service capabilities to support the variety of these customers' needs. 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 mid-sized flavor producers to service this segment. For details regarding Frutarom's flavor activity with medium-sized food and beverage producers, see clause 8.3 below.

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

7.15 Local and global tastes – Taste preferences vary by geographic location and 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. For details regarding Frutarom's geographic reach and its familiarity with local flavors, see clause 8.2 below.

7.16 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, sugar, etc.). Natural products are generally perceived by consumers as being of higher quality, healthier and more environmentally friendly. Similarly, there is growing demand for 'clean label' and organic 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. Frutarom focuses on developing and producing natural products and currently its products consist of more than two thirds natural products. In developed markets, the main growth derives from a shift in consumerism to products considered healthier and more natural, and willingness, even in times of economic slowdown, to continue to purchase these products.

7.17 Private label – private label food 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, with the strengthening of distribution chains and the rise in consumer price conscious, there has been a rise in demand and consumption of private label products, at a higher rate than that of the branded food industry. This trend, accelerated in 2009 as a result of the economic crisis, has continued over the past few years as well, and is expected to continue over the coming years. Consumers, who have tried and had a positive experience with private label products, tend to continue using these. In addition, the increasing power of grocery retailers and their determination to increase their activity margins have lead these to take action in order to strengthen private label product offerings, by allocating greater shelf space and increasing the range of products, among other things. In markets where private labels are especially strong, such as in the UK, private label market share has reached a high of 50%[10]. Furthermore, Supermarket chains and other retailers have also placed greater importance on developing their own brand image. The demand from supermarket chains and retailers for private label products that mimic existing branded products as well as unique premium products has provided the flavors industry with new

[10] Symphony IRI Group, December 2012

opportunities for growth. Frutarom has increased and will continue to increase its market share in the private label market.

7.18 Continuously growing consumption of convenience food – There is an increase in the demand for processed foods with greater convenience (consumed both inside and outside of the home)such as "ready to eat" meals, fresh pasta; ready-to-cook, fresh seasoned or marinated meat or poultry; salads; 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 large market segment.

7.19 Emerging markets – In recent years, certain emerging markets, such as Asia, Central and South America, Central and 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. The Company expects that the continued shift to processed foods and changes in consumer needs in these markets will bring about a continued growth in these markets, at a rate higher than the growth rates expected in developed markets.

Key Success Factors in the Flavor Division

7.20 The Company's management estimates that the key success factors in the Flavors division 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. For details regarding Frutarom's broad global spread, see section 8.2 below.

- Superior and reliable service – The ability to provide a high level of service and the reliability of a flavors manufacturer in providing service are critical for mid-sized, local customers and multinational customers.

- Presence in emerging markets – Many of the emerging markets are growing at considerably higher rates than developed markets. Presence in these key regions, 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.

- Purchase of raw material - There is a growing importance to allocating resources to focused purchase in countries which serve as important sources of many natural raw materials, such as China, India and Brazil, while expanding the choice of suppliers, maximizing the potential to reduce costs through global purchase strengthening relations with raw material manufacturers, processers and growers, mainly natural raw materials, in order to guarantee continuous and reliable supply over time and for improved purchase costs.

8. <u>Products and Services in the Flavor Activity</u>

Frutarom’s Flavor Activity, the most profitable of Frutarom's activities, has been undergoing accelerated growth since 2000. Flavor sales grew from US$26.5 million in 2000 to US$494 million in 2013. Had the four acquisitions made by Frutarom this year been consolidated on January 1, 2013, sales from the Flavor activity would reach US$571 million.

This accelerated growth the result of (a) the strategic focus on the fast growing area of natural food flavors; (b) the development of innovation-based unique solutions combining taste and health for the large multi-nationals; (c) the focus on mid-size and local customers (in emerging and developed markets), with special emphasis on private label companies, providing them with customized services, including technological and marketing support, product development support, tailor-made products, and high level services, as are normally provided to large multi-national companies; and (d) as the result of Frutarom’s strategic acquisitions, which have and are being successfully incorporated into Frutarom's global activities.

8.1 The relative portion of the Flavors Activity out of Frutarom's overall activities grew from 33% in 2000 to 73% in 2013.

8.2 As the success of many of the flavors developed by Frutarom depends on knowledge of local tastes, Frutarom maintains approximately 31 local research and development laboratories in the Flavor's segment and 59 sales and marketing operations in close proximity to its customers in target markets. In addition, Frutarom's global presence enables it to introduce new tastes to local markets. Frutarom's global reach also provides it with the means to service the needs of food and beverage producers launching global brands in many markets simultaneously.

8.3 Frutarom's Flavor Activity provides an efficient, high quality solution to the accelerated demand for private label products, providing assistance and support in developing and marketing the products. Private label manufacturers tend to be mid-sized, local food and beverage producers. Frutarom offers these customers technological support, assistance with the development of products, marketing assistance and a comprehensive product offering, with personalized services suited to each customer's unique needs and flexibility in terms of minimum quantities and lead times Frutarom's acquisitions over the last few years considerably expanded Frutarom's product offering to private label manufacturers, and expanded its global spread, allowing Frutarom to be nearer to its customers.

8.4 Frutarom's Flavor Activity offers a wide variety of flavor products designed to enhance or create new tastes and/or to mask certain tastes in processed foods and beverages.

8.5 Most flavor products consist of numerous raw materials (essences, for example typically contain dozens of raw materials) combined according to formulas developed in the Frutarom's laboratories by the research and development team of the Flavor activity. The development of a new flavor is undertaken either at Frutarom's own initiative or according to the specific requirements of its various customers and in close collaboration with them.

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

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 and juices, dairy and ice cream products, pastries, confectionery, chewing gum, and a variety of savory foods including snacks, soups and salad dressings, as well as processed meat, meat substitutes. Pharmaceuticals and pet food.

8.8 Source – Frutarom offers natural, organic, nature-identical and artificial flavors. The natural compounds are produced only by natural ingredients including natural extracts and essential oils. The nature-identical and artificial compounds are produced also using synthetic ingredients. Some of Frutarom's flavors products contain unique ingredients manufactured by the Company's Specialty Fine Ingredients activity exclusively for the Flavor 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 food. Additionally, Frutarom 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.

8.10 Medium – Frutarom sells its flavor products in stable liquid, paste, powder, emulsion and granulated form and sometimes bundled 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 include fruit, vegetables etc. components, as well as a wide variety of food systems products which do include, among other things, fruit, vegetables and other natural ingredients along with a combination of flavors. The food systems also include sweet and savory sauces such as pizza sauces and salad dressings, ready-to-eat fillings for pasta and other types of ready-to-eat meals, and other preparations made from fruit, vegetables and other natural ingredients used in a wide range of food products, such as dairy (yogurts, ice cream, chilled desserts, butter and cheese), sweet and savory baked products, ready-to-eat meals and other convenience food products. Frutarom's capabilities in the food systems business allows it to combine several fields of its core expertise, as food systems often are produced using flavors, natural flavor extracts and increasingly, natural functional food ingredients manufactured under the Specialty Fine Ingredients activity, allowing it to provide customers with comprehensive, tailor-made solutions.

9. Segmentation of the Income and Profitability of Products and Services

The following are the Group's sales (in US$ thousands) for the years 2011 through 2013, showing Flavor Activity sales and their percentage of the Group's total income:

	2013	2012	2011
Group's total income	673,693	618,001	518,443
Income from Flavors	494,389	457,341	369,894
% of Company's total income	73.4%	74.0%	71.3%

Frutarom's sales in Flavors increased by 8.1% compared with last year, reaching a record high of US$494.4 million, comprising 73% of Frutarom sales, compared with US$457.3 million in 2012.

10. New Products

As part of its Flavors activity, Frutarom is constantly developing a variety of new products. New products are generally developed in cooperation with and adapted to the needs of specific customers. No new product developed by the Company is significant 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, mid-sized, local and small customers. The customers are primarily food and beverage manufacturers and they are located in over 145 different countries worldwide.

11.2 The Flavors activity does not have any one customer who accounts for over 10% of Frutarom's sales turnover (over the last year there have also been no customers whose purchasing turnover was more than 2.2% of Frutarom's sales turnover). The management of the Company estimates that it has no dependency on any one of its customers.

11.3 The majority of sales are made to regular customers since, as previously discussed, the flavor activity is characterized by long-term relationships and customer loyalty. As is customary in the flavor market, there are no long-term supply contracts.

12. Orders Backlog

As is customary in the flavor market, orders are received on an ongoing basis, close to the supply date and therefore orders backlog is not relevant.

13. Competition

13.1 In the flavors market, Frutarom's competitors are 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 service, establishing and maintaining long term customer relationships, 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, when choosing a supplier, customers in this market tend to display low price sensitivity. Flavor manufacturers must differentiate themselves by maintaining close collaborative relationships with customers, thorough knowledge and deep understanding of target markets, high innovative and research and development abilities and must have an established reputation for consistent, reliable and effective provision of services.

13.2 Large multinational flavor manufacturers are established and very experienced companies with a global presence and high technical and commercial capabilities. The large multinational flavor manufacturers with whom Frutarom competes include Givaudan, Firmenich, IFF Inc., Symrise and Takasago.

13.3 The midsized flavor manufacturers with whom Frutarom competes focus on both large multinational food and beverage producers as well as and primarily 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.

13.4 The Company estimates that there are over 500 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 increased market concentration.

13.5 For further information regarding manufacturers acting in the flavor and fragrance market, and Frutarom's position among these, see section 6.3 above. For details regarding the influential factors on the position of the Group in the flavors market, see section 7.15 above ("key success factors in the flavor market").

14. Production Capacity

Production processes in the Flavor activity are relatively simple and do not require significant capital investment, therefore production capacity is not a significant factor nor a restriction on the Company's ability to meet its customers' demands or on its ability to grow in this activity. For more information regarding production capacity see section 26 of this report.

Specialty Fine Ingredients Market

15. Overview of the Fine Ingredients Market

General

15.1 The specialty fine ingredients market in which the Company operates produces ingredients 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, pharmaceutical/nutraceutical, cosmetics and personal care industries. Fine ingredients are often sold directly to food and beverage manufacturers who use them in the manufacture of consumer end products. Flavor and fragrance manufacturers use fine ingredients products as the building blocks for the flavor and fragrance compounds they manufacture.

15.2 Frutarom operates in the following fields of the specialty fine ingredients market: natural flavor extracts, natural functional food ingredients, natural pharmaceutical/nutraceutical extracts, specialty essential oils, algae and citrus products, aroma chemicals, and natural gums.

15.3 According to an estimate by Koncept Analytics[11], the sales of specialty fine ingredients to the food and beverage industries in the world (including sales of flavor and other raw materials) are expected to grow at an annual rate of 7.3% during the years 2012 – 2016.

Characteristics of the Fine Ingredients Market

15.4 Research and development – Innovation is a key success factor in the fine ingredients market. Research and development of new fine ingredients products is a sophisticated process that requires a high level of expertise, experience and investment. In many cases, the development of new fine ingredients products takes longer than that of flavor products. Some of the natural fine ingredients are tailor-made to customer needs and require long-term relationships with the customers and collaborative development efforts.

15.5 Production – The production of fine ingredients tends to be more sophisticated and complicated than the production of flavors, requiring extensive knowhow. In addition, the production of fine ingredients requires greater capital investment in the construction of manufacturing facilities, as well as in increasing production capacity

[11] Koncept Analytics, November 2013

when required. The production of fine ingredients must also comply with stricter environmental and regulatory standards.

15.6 Supply chain – Customers are increasingly seeking to optimize their inventory level, therefore requiring fine ingredients manufacturers to meet shorter lead times and to keep local stocks in main markets. In addition, mid-sized and local customers purchase hundreds of fine ingredients in variable, relatively small quantities. The large multinational fine ingredients manufacturers often have strict policies of minimum quantity and standardized packaging, while small fine ingredients manufacturers generally do not have the operational flexibility and the required global supply chain to meet the needs of many mid-sized customers. This has created a market opportunity for mid-sized fine ingredients producers.

15.7 High barriers to entry– An established reputation and brand recognition, which can only be developed over time are key success factors for manufacturers in the fine ingredients market. Food and beverage producers require a high degree of reliability and consistency, and once an ingredient is incorporated into a product, producers rarely risk replacing the fine ingredients supplier in order to avoid an adverse effect on the quality of that product. In addition, building a competitive advantage of a multinational fine ingredients manufacturer requires compliance with stringent supervisory, regulatory and environmental demands as well as strong research and development, production and global supply chain capabilities, including capital investments in construction of production facilities and increasing the production capacity when and if necessary. These factors create significant entry barriers.

15.8 Growing demand for natural products – The rise in consumer demand for natural products has in turn increased demand that a variety of fine ingredients, such as natural flavor extracts and natural specialty essential oils, be used in such products. Natural fine ingredients tend to be more unique and less interchangeable, resulting in greater customer loyalty. Many of the natural extracts and specialty essential oils are tailor-made to customer needs. Frutarom focuses on the development of natural products, providing a solution to this growing global consumer trend. For further details, see section 16.5 below.

15.9 Growing demand for functional food ingredients – Functional food is food with certain added ingredients which provide, or are perceived as providing, health benefits, such as juices or milk products with health additives. Changing consumer preferences lean towards food with health advantages, leading to increasing demand for functional food. The end user markets of the functional food industry exhibiting the highest growth are the dairy and beverage markets. Many of the active ingredients used in functional foods are derived from plants and herbs using similar production processes as those used in the production of flavor extracts. Functional food ingredients manufacturers are often required by food and beverage producers to provide a scientific basis for the health claims attached to such functional food ingredients, such as clinical studies.

15.10 Regulatory, health safety and certification – The fine ingredients used in the food, beverage and pharmaceutical/nutraceutical industries are increasingly subject to strict health and safety regulations. At the end of 2006, REACH regulations were published in the EU detailing the registration arrangements, assessments, certifications and restrictions on all chemicals produced in or imported into the European market. In December 2008 the EU adopted a new regulation prescribing definitions, labeling requirements and maximum quantities of BAP's (Biologically Active Principles), which came into force on January 20, 2011. In January 2009 the European Union adopted regulation 1334/2008 on the matter of flavors, defining natural products and the manner of labeling such. This regulation went into effect on January 20, 2011.

Customers of raw materials in general and specialty fine ingredients in particular often require their manufacturers to provide certification that their products meet strict regulations and standards. In addition, there is increasing demand for products with certain proven qualities, such as genetically modified organism free ("GMO-free") or products that are pesticide free. Kosher and Halal certified products are also increasing in demand by a wider demographic customer base. As a result, fine ingredients manufacturers are increasingly required to document their manufacturing processes and to adhere to strict standards in order to ensure compliance with such certification requirements. Lastly, fine ingredients manufacturers are expected to be approved by various manufacturing standards such as ISO 9001, Swiss GMP, ISO 22000 and BRC Version 6 (British Retail Consortium).

Frutarom's specialty fine ingredients comply with strict health, safety and quality standards. For further details, see section 16.4 below.

15.11 Sourcing – in order to maintain a high level of product quality and consistency and to ensure the availability of raw materials used for the production of the specialty fine ingredients, as and when needed for production, long term relationships with suppliers, growers and/or producers of raw materials are of crucial importance to the specialty fine ingredients manufacturers. This is the case particularly for natural raw materials, which are mostly crop-related goods and are often subject to seasonality in supply.

15.12 Production of high volume of fine ingredients with low margins – during recent years, there has been an increase in the production of certain fine ingredients, in certain countries such as China and India, where the cost structure is lower for manufacturers. A large number of these manufacturers tend to have less technical sophistication and research and development capabilities, and they focus more on higher volume, lower margin fine ingredient products. In addition, they tend not to have global sales and marketing capabilities, brand recognition or approved supplier status. This has led certain fine ingredients' manufacturers to set themselves apart from these low-cost manufacturers, by developing close, collaborative relationships with customers, providing higher added-value products and services, and investing in research and development in order to develop higher margin, specialty fine ingredients products.

Key Success Factors in the Fine Ingredients Division

15.13 The Company's management estimates that the key success factors in the Fine Ingredients division are:

- Positioning and reputation as a reliable supplier – it is extremely important to have reliable service and to build up a reputation as a supplier in the market.

- New, innovative and comprehensive product portfolio – in the fine ingredients market, it is very important to have new, innovative, added-value products that satisfy consumer demand.

- Innovation in research and development – suppliers must have strong research and development and innovation competencies to supply innovative products such as functional food ingredients, and to adapt products, mainly natural, to customer needs.

- Compliance with quality, regulatory and safety standards – since fine ingredients are intended for the food and beverage and pharmaceutical/nutraceutical markets, which provide health benefits apart from taste, they must comply with strict quality, regulatory and safety standards.

- Raw material procurement – there is a growing importance to allocating resources to focused procurement in countries which serve as important sources of many natural raw materials used for the production of specialty fine ingredients, such as China, India and Brazil, while expanding the choice of suppliers, maximizing the potential to reduce costs through global purchase and strengthening relations with raw material manufacturers, processers and growers, mainly natural raw materials, in order to ensure continuous and reliable supply of raw materials over time and improvement of purchasing cost. Locating quality raw materials and the right timing for the purchase of these is the key to maintaining timely and stable supply for customers and for keeping up with the changing demands in quantity and quality.

- Wide geographic reach to support and service multinational customers – The wide geographic reach of the Company providing multinational customers support and ongoing assistance during working hours, in the language of the customer and its location, is imperative.

16. Products and Services in the Fine Ingredients Activity

16.1 Under the Fine Ingredients activity, Frutarom develops, manufactures, markets and sells natural flavor extracts, natural functional food ingredients, natural pharmaceutical/nutraceutical extracts, specialty essential oils and citrus products, aroma chemicals, natural gums and more.

16.2 Specialty Fine Ingredients sales grew substantially from US$49 million in 2000 to US$145.6 million in 2013. The growth in Specialty Fine Ingredients sales results mainly from the development of new and innovative products focus on both multinational customers and mid-sized local customers and from the strategic acquisitions successfully executed. The portion of Specialty Fine Ingredients sales out of Frutarom's total sales totaled 21.6% in 2013. Specialty Fine Ingredients are sold primarily to the food and beverage, flavor and fragrance, pharmaceutical/nutraceutical, cosmetics and personal care industries.

16.3 Frutarom has an established reputation in the market for fine ingredients, with a broad customer base of multinational, mid-sized and local customers supported by Frutarom's sales and marketing team and efficient global supply chain. The Company has local warehouses in Europe, USA, Central and South America and Asia allowing it to supply its products to its customers in a timely manner, in most cases, within several days. Although the majority of the fine ingredients produced by the Company are sold to third parties (including competing flavor manufacturers), a portion of Frutarom's fine ingredients production is used for its Flavor activity, and some unique raw materials, such as citrus products and natural health products, are used solely by the Company for the development and creation of unique flavor and health solutions, giving Frutarom a competitive advantage.

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16.4 Frutarom's specialty fine ingredients meet strict health, safety and quality standards, such as ISO 22000, FSCC 22000, Swiss GMP, British BRC and ISO 9000 standards. Frutarom's fine ingredients are also generally GMO-free and pesticide free, and satisfy a variety of Kosher and Halal certifications.

16.5 Frutarom focuses on the development of natural products, providing a solution to the growing global consumer trend of natural products consumption, which is considered healthier. Frutarom's management believes that the Company is one of the world leaders in this market and successfully uses its experience of over 80 years of research, development and production of natural and unique specialty fine ingredients, allowing it to offer a wide variety of products based on a global, efficient supply chain. Frutarom's in-depth knowledge of the flavors market and its knowledge of customer demand in the food industry, and of specialty fine ingredients, places Frutarom at a unique meeting point allowing it to provide solutions combining both flavor and health.

16.6 Frutarom believes that its relationship with and understanding of food and beverage markets provide it with a competitive advantage in the functional food ingredients market. This is complemented by Frutarom's research and development capabilities, proprietary production technologies and clinical study capabilities.

As stated, Frutarom's Specialty Fine Ingredients division is divided into several main categories:

16.7 **Natural Flavor Extracts** – Frutarom is a leading manufacturer of a wide variety of natural flavor extracts which are extracted from fruit, plants and other botanical materials Frutarom's main customers for natural flavor extracts are food and beverage producers, flavor and fragrance companies (including the Company's own Flavors activity) and, to a lesser extent, tobacco companies. The natural flavor extracts are generally tailor made products and the Company works in close collaboration with customers to create the exact flavor extract required.

16.8 **Natural Functional Food Ingredients** – The Company offers a variety of standardized natural extracts used as raw materials in the manufacture of functional food. Functional foods are foods which include additional specialty fine ingredients which provide health benefits. Functional food ingredients are subject to different requirements, but at the same time are subject to fewer restrictions than pharmaceutical/nutraceuticals. The main customers for the Company's functional food ingredients are food and beverage producers.

16.9 **Natural Pharmaceutical/Nutraceutical Extracts** – Frutarom manufactures a variety of standardized natural extracts with certain medicinal and health benefits used in the manufacture of prescription drugs, over the counter pharmaceutical products and natural dietary supplements. The main customers of the pharmaceutical/nutraceutical extracts are pharmaceutical companies, nutraceutical and dietary supplement producers.

16.10 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 citrus (such as orange, grapefruit, lemon and mandarin), mint (peppermint and spearmint), floral, seasoning, herb and woody oils. These products are used in food and beverages, flavor and fragrance applications, pharmaceutical products, cosmetics and other wellness and personal care applications.

The Company's management estimates that Frutarom is the global leader in specialty citrus products used to infuse citrus flavors into food, beverages, fragrances and other personal care products. Frutarom has been active in the production of citrus specialties since 1933. The Company continuously invests in innovative and unique technologies for processing, extraction and distillation of specialty citrus products. In February 2014 Frutarom acquired the activity of CitraSource, which specializes in research and development, production, marketing and sale of specialty citrus. CitraSource has a state of the art plant in Florida, and global purchase capacities in citrus which will strengthen Frutarom's leadership position in the market of development, production and selling of citrus specialty products. A number of Frutarom's citrus specialty products are reserved for the exclusive use of the Flavors activity and are not sold to third party flavor manufacturers, providing the Company with a competitive advantage in the production of citrus flavors. For further details regarding the acquisition of CitraSource, see the Company's immediate report dated February 25, 2014.

16.11 Aroma Chemicals – Frutarom produces over 700 different types of aroma chemicals used in the manufacture of flavor and fragrance compounds, food, animal feed, cosmetics, oral hygiene products and other applications. Frutarom is a leading global player in the field of unique aroma chemicals, focusing on research and development, manufacturing and selling of high-added-value specialty aroma chemicals, with a continuous trend in product mix towards low volume, high margin products. Frutarom's range of aroma chemicals used in flavor and fragrance applications includes diketones and pyrazines, used to create roasted and toasted aromas. In addition, Frutarom manufactures unsaturated aldehydes, cooling agents designed to impart a cool sensation when orally consumed or applied to the skin, used in the manufacture of candies, chewing gum, skin care products and oral hygiene products, among others.

16.12 Natural Gums – Frutarom offers a range of natural water soluble gums and stabilizers derived from a variety of botanical sources, including certain types of gum trees, seeds, seaweed and beet sugar. The natural water soluble gums and stabilizers are used in the production of food, beverages, pharmaceuticals and cosmetics. The main customers are producers of food, beverages and flavors, and pharmaceutical companies.

16.13 **Algae** – Over the past few years Frutarom, together with the Ben Gurion University of Israel, has invested in research and development related to algae, considered worldwide to be an attractive food additive (a source of Omega 3), medicinal extracts and components in various cosmetic products. The specialty algae is grown for productions purposes on an agricultural farm in the south of Israel. Frutarom extracts the active ingredients from the algae using natural processes, and markets these to food, dietary supplement, cosmetics and personal care companies throughout the world.

17. Segmentation of the Income and Profitability of Products and Services

The table below presents data on the Group's sales (in US$ thousands) for the years 2011 through 2013 deriving from the Specialty Fine Ingredients activity and from the Aroma Chemical products, and its portion of the Group's total income:

	2013	**2012**	**2011**
Group's total income	673,693	618,001	518,443
Income from Specialty Fine Ingredients	145,591	140,763	145,008
% of income from Specialty Fine Ingredients	21.6%	22.8%	28%

18. New Products

Frutarom develops new Specialty Fine Ingredients as part of its ongoing activity in order to strengthen its position and improve its product diversity, including by replacing low profit margin products with innovative, added-value products with higher profit margin. No single new product is significant from the aspect of forecasted sales turnover and/or development expenses.

19. Customers

19.1 The Specialty Fine Ingredients manufactured by Frutarom are sold to a large customer base that includes many large multinational, mid-sized, local and small customers in the food and beverage, pharmaceutical/nutraceutical, flavor, fragrance and personal care industries.

19.2 The Specialty Fine Ingredients activity has no one particular customer which accounts for over 10% of the Group's sales turnover(over the last few years there have also been no customers whose purchasing turnover was more than 2% of Frutarom's sales turnover). The Company's management believes that it is not dependent on any of its customers.

19.3 Excluding a number of supply contracts for periods not exceeding one year, most sales are made on the basis of specific purchase orders by customers and based on the Company's forecast. Sales are mainly to regular customers with long-term relationships.

20. Order Backlog

As customary in the specialty fine ingredients market, orders are received on an ongoing basis close to the supply date and therefore orders backlog is not relevant. There are a number of supply agreements for periods not exceeding one year, none of which are significant relative to the Company's overall activity.

21. Competition

21.1 In the market for specialty fine ingredients, competition varies by product category.

21.2 In the natural flavor extract category, the Company's competitors are manufacturers that specialize in natural flavor extracts, such as Naturex, pharmaceutical/nutraceutical manufacturers and multinational and mid-sized manufacturers that produce specialty fine ingredients, mainly for internal use, such as Givaudan, IFF, Symrise, Sensient, Robertet and Mane.

21.3 In the functional food ingredients and pharmaceutical/nutraceutical extracts category, Frutarom's competitors are mainly specialized pharmaceutical/nutraceutical companies such as Indena S.p.A., Naturex, Martin Bauer GmbH & Co. and KG, as well as a number of small start-up companies that specialize in unique and innovative products and technologies.

21.4 In the essential oils category, Frutarom's competitors include companies such as Treatt plc which focus on the manufacture of essential oils, including specialty essential oils, and large multinational and mid-sized flavor manufacturers that produce specialty essential oils primarily for internal 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 market for essential oils.

21.5 In the aroma chemical category, the Company competes with large multinational flavor manufacturers who produce specialty aroma chemicals for internal use. Additional competitors in this field are specialized aroma chemicals manufacturers such as Aromor, Fontarome and Bedoukian Research. Other manufacturers of aroma chemicals are generally low cost local producers, located mainly in Asia. These manufacturers have direct and limited sales and marketing infrastructures, and they are often reliant on traders for the purpose of marketing and selling their products. There are also large chemical companies that manufacture high volume aroma chemicals as part of their wider product offering but in most cases do not offer specialty aroma chemicals. For the most part, Frutarom does not compete with these low-cost producers as it focuses on higher profit margin specialty aroma chemicals whose scope is not substantial, with relatively high profit margins.

21.6 For further information regarding manufacturers acting in the specialty fine ingredients market, see section 6.3 above. For details regarding the factors affecting the Group's position in the specialty fine ingredients market, see section 15.13 above ("Key success factors in the specialty fine ingredients market").

22. Production Capacity

For information on production capacity see section 26 of this report.

23. Frutarom's Trade and Marketing Activity

23.1 As stated above, Frutarom has additional activity in the field of importing and marketing of certain raw materials produced by third parties in the food, pharmaceutical, chemicals, cosmetic, and detergent industries as part of its service and comprehensive solutions it offers its customers, aid it in the strengthening of relations and promotion of sales of its core products and helping sustain significant and long lasting relations with customers.

23.2 The raw materials sold and marketed by Frutarom under the Trade and Marketing activity are mainly raw materials that Frutarom imports for the manufacture of its specialty fine ingredients and flavors. As Frutarom imports and purchases these materials in bulk or in large quantities, it is able to purchase these materials at attractive prices and sell them at a premium to third parties. The Trade and Marketing activity is synergetic to Frutarom's core business – Flavors and Specialty Fine Ingredients – as it leverages the Company’s existing sales systems, supply chain and global systems.

23.3 Trade and Marketing activity is not part of Frutarom's core business. In 2013 this activity totaled US$39.7 million. In view of the fact that this activity is not significant to Frutarom, it is not dealt with separately in this report.

CHAPTER 4 – DESCRIPTION OF THE COMPANY'S BUSINESS: MATTERS RELATING TO THE COMPANY'S OVERALL ACTIVITY

24. Marketing and Distribution

24.1 Frutarom maintains a global marketing, sales and customer technical support organization. This organization is based on local R&D, sales and marketing personnel in its key target markets. The Company estimates that its global presence provides it with a competitive advantage and is a key factor in the success of its growth strategy. On December 31, 2013, Frutarom had 1,043 sales, marketing and R&D professionals, 68 sales and marketing offices and 37 research and development laboratories located in its target markets in close proximity to its customers, including in the US, Brazil, Costa Rica, Mexico, the UK, Germany, Switzerland, France, Italy, Slovenia, Norway, Denmark, Israel, Russia, Ukraine, Turkey, Kazakhstan, Romania, Czech Republic, China, Vietnam, Japan, Hong Kong, Indonesia, India, Nigeria, South Africa, Belgium, Guatemala, Macedonia, Holland, Poland, Serbia and Slovakia. The Company markets and sells its products primarily through its own sales personnel. In certain countries, Frutarom retains third party agents and distributors to sell its products.

24.2 Frutarom's global sales and marketing organization is a key component of its strategy to provide tailor-made specialized products and services and high quality customer support to both large multinational and mid-sized and local customers.

24.3 Frutarom differentiates itself from its major competitors, among others things, by offering its mid-sized and local customers the same quality of service and tailor-made product specialization that it offers large multinational companies. Frutarom's sales and marketing personnel and its research and development personnel work equally closely with both large multinational and mid-sized and local companies to offer timely and accessible personalized development services, including custom flavors development and specialty fine ingredients tailor made to the customer's specific needs. The Company estimates that the mid-sized and local customer segment represents more than 60% of the global food and beverage market.

24.4 The Flavor and Specialty Fine Ingredients activities each have their own separate sales, marketing and customer support personnel. However, Frutarom assigns one dedicated salesperson to any customer purchasing the products of both activities. This single-sales person interface allows Frutarom to better respond to its customers' needs and to identify and realize selling opportunities of its variety of products to the same customer.

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

24.6 Frutarom's marketing and sales team form an important link between Frutarom's customers and its research and development team. Working closely with customers is necessary in order to understand their specific needs while relaying this information in full cooperation to the research and development team, which, in turn develops tailor-made products for such customers' specific needs, in some instances in close cooperation with the customer's research and development team.

24.7 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 that this approach further strengthens its relationships with these customers and helps to increase demand for its products.

24.8 The Group's management estimates that it does not depend on any one of its marketing channels.

25. Seasonality

25.1 The Company's business is affected by seasonal fluctuations, which until recently were reflected in higher sales and profitability in the first half of any given year, and lower sales and profitability during the second half of any given year (particularly in the fourth quarter of each year). A substantial portion of the Company's products is used by its customers in the manufacture of beverages and milk products such as soft drinks, ice cream and yogurt, for which demand increases during the summer months. As a result, the Company's sales of certain flavors and raw materials increase over the first half of the year, as beverage and milk product manufacturers increase inventories and production in advance, in anticipation of increased demand in the summer months.

25.2 The impact of seasonality fluctuations on the Company's results and activities have become less pronounced over the last few years, with the increase in sales of products such as savory flavors, functional food ingredients and natural extracts from medicinal plants, targeted for the pharmaceutical/ nutraceutical industry, which are less impacted by seasonal demand.

25.3 The acquisition of PTI, which specializes mainly in savory flavors and fine ingredients (including to the processed meat industry), where demand increases in the winter, is expected to bring about a certain change in Frutarom's seasonality mix, as PTI sales are highest in the fourth quarter and lower in the first quarter.

25.4 The following is the quarterly profit and loss reports for 2012-2013:

	Q4 2013	Q3 2013	Q2 2013	Q1 2013	Q4 2012	Q3 2012	Q2 2012	Q1 2012
Income	191.8	161.0	168.6	152.2	144.9	157.1	164.8	151.2
Gross profit	70.2	62.3	66.9	57.2	51.5	58.1	61.8	54.9
R&D, Sales, Management & General expenses	49.9	40.0	42.0	38.3	37.8	38.5	40	37.1
Operating profit*	20.4	22.6	24.9	18.9	13.7	19.5	21.8	17.8
EBITDA*	28.3	29.4	32.5	25.8	20.7	26.3	28.5	25.0
Finance expense	2.5	1.3	2.3	1.4	1.4	0.6	4.3	0.9
Profit before tax	17.8	21.3	22.6	17.5	12.3	18.9	17.5	16.9
Net profit	15.0	17.0	17.6	14.0	10.5	14.4	13.5	13.5

* One-time expenses in the amount of approximately US$5.1 million affected operating profit in 2013 (reorganization expenses of US$2.5 million, and adjustments and acquisition expenses of US$2.6)

26. Fixed Assets, Facilities and Production Capacity

As of the date of publication of this report, Frutarom has 33 production facilities around the world. The following table sets forth Frutarom's major production facilities and the activity at each of them:

Country	Location	Field of Activity	Size of property (m^2)	Buildings Ownership/Lease	Land Ownership/ Lease/ Rent
Israel	Haifa[12 14]	Flavors and fine ingredients	35,490	Ownership	Lease
Israel	Acco [11]	Flavors	9,273	Ownership	Lease
Switzerland	Wadenswil	Fine ingredients	13,464	Ownership	Ownership
Switzerland	Reinach	Flavors	43,000	Ownership	Oownership
Germany	Emmerich	Flavors	19,000	Ownership	Ownership
Germany	Sittensen	Flavors	10,001	Ownership	Ownership
Germany	Stuttgart (Gewurzmuller)[15]	Flavors	13,600	Lease	Rent
UK	Hartlepool	Fine ingredients	31,971	Ownership	Ownership
UK	Wellingbourough	Flavors	8,090	Ownership	Ownership
USA	North Bergen (NJ)	Fine ingredients	32,000	Ownership	Ownership
USA	Corona (CA)[16]	Flavors	14,000	Rent	Rent

[13] Frutarom Ltd. owns land rights in Haifa Bay and Acco industrial areas. The net capitalized leasing fee for the land is in the amount of approximately US$ 1,109 as at December 31, 2012 (US$1,141K as at December 31, 2011). Land leasing rights are granted for a period of 49 years ending during the years 2032 – 2042. Frutarom Ltd has the right to extend the lease 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 Administration (excluding that stated in footnote 12 below). The capitalized lease fees are presented in the financial reports under fixed assets.

[14] The total size of the Haifa site is approximately 35.5 dunam including a rented space under an operating lease with a third party totaling 7.3 dunam until February 2015. The annual leasing fee for 2011 is NIS 810,000. The annual leasing fee for 2012 is NIS 780,000 a year. Annual lease fees for 2013 were NIS990 thousand.

[15] The land and facilities 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 on October 1, 2017. The annual rental fee is EUR 600,000 a year (EUR 544,000 for the GewurtzMuhle plant and EUR 56,000 for the plant in Blessing). According to the lease, the Company has a unilateral option to extend the rental agreement by another 5 years. If the option is realized, rental fees will be updated according to the amount customary in the market at the time being for the rental of similar assets, and the price will be adjusted to the changes in the German Consumer Price Index. At the end of the rental period, the agreement will be extended automatically by additional periods of two years each, until one of the parties notifies regarding termination of the agreement, at least one year in advance. The Company is entitled to terminate the contract by one years' advance notice.

Country	Location	Field of Activity	Size of property (m^2)	Buildings Ownership/Lease	Land Ownership/ Lease/ Rent
USA	Cincinnati (Ohio)	Flavors	57,000	Ownership	Ownership
USA	Branchburg, NJ	Flavors	38,800	Rent	Rent
USA	Winter Haven (Florida)	Specialty fine ingredients	68,000	Ownership	Ownership
China	Kunshan [17]	Flavors	15,000	Ownership	Leasing
Italy	Parma	Flavors	7,500	Ownership	Ownership
Slovenia	Škofja-Etol	Flavors	65,000	Ownership	Ownership
Brazil	Porto feliz/ 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

The facilities and properties owned by the Group are presented in the financial reports as the Group's fixed assets in the section on land and facilities. All of the Group's lease agreements are defined as operational lease and are therefore not included and presented under assets.

The Company also has production facilities which are not significant in proportion to the Company's scope of activity. Following is a description of the Company's significant plants:

- **Haifa, Israel** – In the Haifa plant, the Company produces flavors and fine ingredients (specialty essential oils, specialty citrus products and aromatic chemicals). The plant also contains management offices.

  Production capacity and shifts – Flavor production is performed five days a week with one shift per day. The plant has additional potential production capacity of approximately 100%, assuming three shifts per day. Fine Ingredients at the plant is performed five days a week in three shifts per day.

[16] The property and the facilities of the Company's plant in Corona are rented by Company from a third party under a 6 year rental agreement ending on February 28, 2015. The annual rental fee is US$ 200,000. According to the lease, the Company has a unilateral option to extend the agreement by another 4 years for a rental fee that will be adjusted to the market price on March 1, 2014.

[17] An associated company in China has rights of use of land for a period of 50 years, ending in 2046. Net capitalized lease fees for said property are US$1167 thousand as of December 31, 2013 (US$178 thousand as of December 31, 2012). Capitalized lease fees are presented in the statements as permanent assets

- **Acco, Israel** – The Company produces flavor mixes (mainly savory flavors) at the plant in Acco.

  Production capacity and shifts – Production at the plant is performed five days a week in one shift. The plant has additional potential production capacity of 100% assuming three shifts per day.

- **Wädenswil, Switzerland** – At the Wädenswil plant the Company's Flavor activity produces natural extracts for the Specialty Fine Ingredients activity.

  Production capacity and shifts –The plant works five days a week in two shifts. The plant has additional potential production capacity of about 30%-40% assuming continuous production over seven days a week in three shifts.

- **Reinach, Switzerland** – At this plant the Company's Flavor activity produces mainly food systems, mainly as part of the Flavor activity.

  Production capacity and shifts –The plant works five days a week with approx. two shifts each day. The plant has additional potential production capacity of about 20%-25% assuming continuous production in three shifts.

- **Emmerich, Germany** – At this plant the Company's Flavors activity are mainly production of food systems.

  Production capacity and shifts – The plant works five days a week in approx. two shifts. The plant has additional potential production capacity of about 30%-35% assuming continuous production in three shifts.

- **Sittensen, Germany** – At this plant the Company's Flavor activity produces savory flavor mixes and seasonings.

  Production Capacity and shifts – the plant works five days a week, in two shifts. The plant has additional potential production capacity of 25%- 30% assuming continuous production in three shifts.

- **Korntal, near Stuttgart, Germany (Gewurzmuller)** – At this plant the Company's Flavor activity produces savory flavor mixes and seasonings.

  Production capacity and shifts – The plant operates 5 days a week with one shift. The plant has additional potential production capacity of around 100% assuming continuous production in three shifts.

- **Wellingborough, UK** – At this plant the Company's Flavor activity produces flavors.

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

- **Hartlepool, UK (Oxford)** – At the Hartlepool plant, the Company's Specialty Fine Ingredients activity produces aroma chemicals.

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

- **North Bergen, New Jersey, USA** – At this plant the Company produces natural plant extracts and natural gums in the 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 35%-40% assuming continuous production with three shifts, 7 days a week.

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

  Production capacity and shifts – The plant works 5 days a week with 1 shift during most of the year and 1.5-2 shifts during the summer months. The plant has additional potential production capacity of approximately 60% - 70% assuming production in three shifts.

- **Cincinnati, USA (Flavor Systems site)** - At this plant in Cincinnati, Ohio, the Company’s Flavor activity produces flavors.

  Production capacity and shifts – The plant works 5 days a week, one shift during most months of the year, and one and a half to two shifts during the summer months. The plant has additional potential production capacity of about 60% - 70% assuming continuous production of three shifts.

- **Branchburg NJ, USA (Hagelin site)** – At this plant the Frutarom manufactures flavors and technologies, as part of its flavors activity.

Production capacity and shifts – The plant works five days a week in one shift. The plant has additional potential production capacity of 100% if it goes over to continuous production.

- **CitraSource, USA (Florida plant)** – at this site Frutarom manufactures specialty taste solutions and citrus specialty flavors (including citrus oils) – oranges, lemons, grapefruits and tangerines. The plant's activities also include a refrigerated tank farm for storing different types of raw materials, mainly citrus.

  Production capacity and shifts – The plant works five days a week in one shift. The plant has additional potential production capacity of 100% if it goes over to continuous production of three shifts.

- **Kunshan, China** – At this plant the Company's Flavor activity produces flavors.

  Production capacity and shifts – The plant works five days a week with one shift. The plant has additional potential production capacity of approximately 100% assuming production in shifts.

- **Parma, Italy -** At this plant in Parma, the Company's Flavor activity produces savory flavor mixes.

  Production capacity and shifts – The plant works 5 days a week, one shift. The plant has additional potential production capacity of about 100 % if it shifts to continuous production of three shifts.

- **Škofja vas, Slovenia** - At this plant in Škofja vas, the Company's Flavor activity produces mainly flavors, beverage bases, food systems and savory flavor mixes.

  Production capacity and shifts – The plant works 5 days a week, 1.5 shifts. The plant has additional potential production capacity of about 40%-50%

- **Porto Feliz, Brazil (Sao Paulo) -** At this plant in Porto Feliz, the Company produces essences as part of its Flavor activity.

  Production capacity and shifts – The plant works 5 days a week, one shift. The plant has additional potential production capacity of about 100% in flavors if it shifts to continuous production of three shifts.

- **Guatemala City, Guatemala (Aroma site)** – At this plant the Frutarom manufactures flavors (mostly sweet) for beverages, milk products, sweets, snacks and more,, as part of its flavors activity.

  Production capacity and shifts – The plant works 5.5 days a week in one shift. The plant has additional potential production capacity of 100% if it goes over to continuous production of three shifts every day.

- **<u>Moscow, Russia (PTI – Platinum Absolut site)</u>** – At this plant the Frutarom manufactures spice mixes and functional raw materials for the food industry, as part of its flavors activity.

  <u>Production capacity and shifts</u> – The plant works five days a week in one shift. The plant has additional potential production capacity of 100% if it goes over to continuous production of three shifts.

27. <u>Research and Development</u>

27.1 Frutarom considers its research and development system to be one of its key competencies, and focuses and invests great resources in the research and development of new and innovative products. As at December 31, 2013, Frutarom employs about 365 research and development employees. Frutarom has over 80 years of experience in research and development in the field of flavors and specialty fine ingredients, particularly natural flavors and natural fine ingredients. Frutarom's research and development activities are crucial to its success, as many of its products, particularly natural products, are tailor-made to customers' specific needs. As part of Frutarom's research and development activities and in order to broaden its offering of natural, innovative and unique products, Frutarom works to create collaborations with leading academic institutions, research institutes and start-ups throughout the world. Frutarom has created a number of such collaborations that strengthen and broaden the pipeline of new and innovative products it intends to launch in the coming years.

27.2 The development of fine ingredients is in many cases Frutarom's own initiative, based on its assessment of market trends and needs while focusing on developing products with higher margins in order to continue and improve the Company's product mix and optimize production capabilities and capacity.

27.3 The development of new and customized flavor products is a complex process calling upon the combined knowledge of the Company's scientists and flavorists. Scientists from various disciplines work in project teams that include flavorists to develop flavors with consumer preferred performance characteristics. The development of new flavor compounds is as much an art as it is a science, requiring in depth knowledge of the flavor characteristics of the various ingredients used and is, to a large extent, conducted as a trial and error process.

27.4 As of the date on which this report was published, the Flavors activity has approximately 31 research and development laboratories. The main laboratories are located in the UK, Switzerland, Germany, the US, Slovenia, Israel, Russia, Italy, Turkey, China, Brazil and South Africa. In the Fine Ingredients field, Frutarom has approximately 10 research and development facilities located in Israel, the UK, Switzerland the US, China and the Netherlands.

27.5 The Company recognized all research and development expenses at the time of occurrence as an expense in the financial reports. For details, see Note 2f (6) and Note 20(b) in the Financial Reports.

27.6 For further information regarding the liabilities recognized in the financial reports as grants and amounts that were attributable to research and development expenses, see Note 2.f and 6 and Note 11 a.2 of the financial reports.

28. Intangible Assets

28.1 Frutarom’s intellectual property includes mainly of the formulas used to create its flavors and production processes for the development and production of fine ingredients. These formulas are not registered as patents but are highly confidential proprietary business information, available to a limited number of people within the Group. The protection of formulas as trade secret rather than registering them as patents is common industry practice , as doing so would make the formulas publicly known and the protection and the patent protection would only be available to a given flavor producer for the life of the patent. Additionally, the Company has registered patents, mainly relating to the manufacturing processes of ingredients that were developed by the Group and relating to certain pharmaceutical/nutraceutical products. The Company also registers trademarks for some of its products in some of the countries in which it operates. In order to protect its intellectual property rights, the Company includes certain confidentiality, non-competition and transfer of intellectual property rights in its personal agreements with employees and consultants, and in agreements with suppliers and customers. Frutarom does not consider itself to be materially dependent on any single intellectual property right, proprietary formula, patent or license.

28.2 The Company has not registered the "Frutarom" trademark in all of the jurisdictions in which it currently operates. In certain such jurisdictions, trademarks substantially similar to "Frutarom" for goods similar to the Group products have already been registered by third parties. The Company's management estimates that not registering the "Frutarom" trademark in all the jurisdictions in which it operates does not constitute a significant risk to the Group and its activities.

28.3 For details regarding amounts recognized as assets in the Financial Reports for intangible assets, see Note 5 and Note 8 of the Financial Reports.

28.4 The reduction of intellectual property, representing know-how and formulas, is performed according to Group management's assessment relating to the length of time such know-how will be utilized, in light of the fact that most of the know-how and formulas have no technical or regulatory statute of limitations, and in light of the Group's experience regarding periods of use of the Group's know-how and formulas, according to the industries in which the Group operates.

29. Human Resources

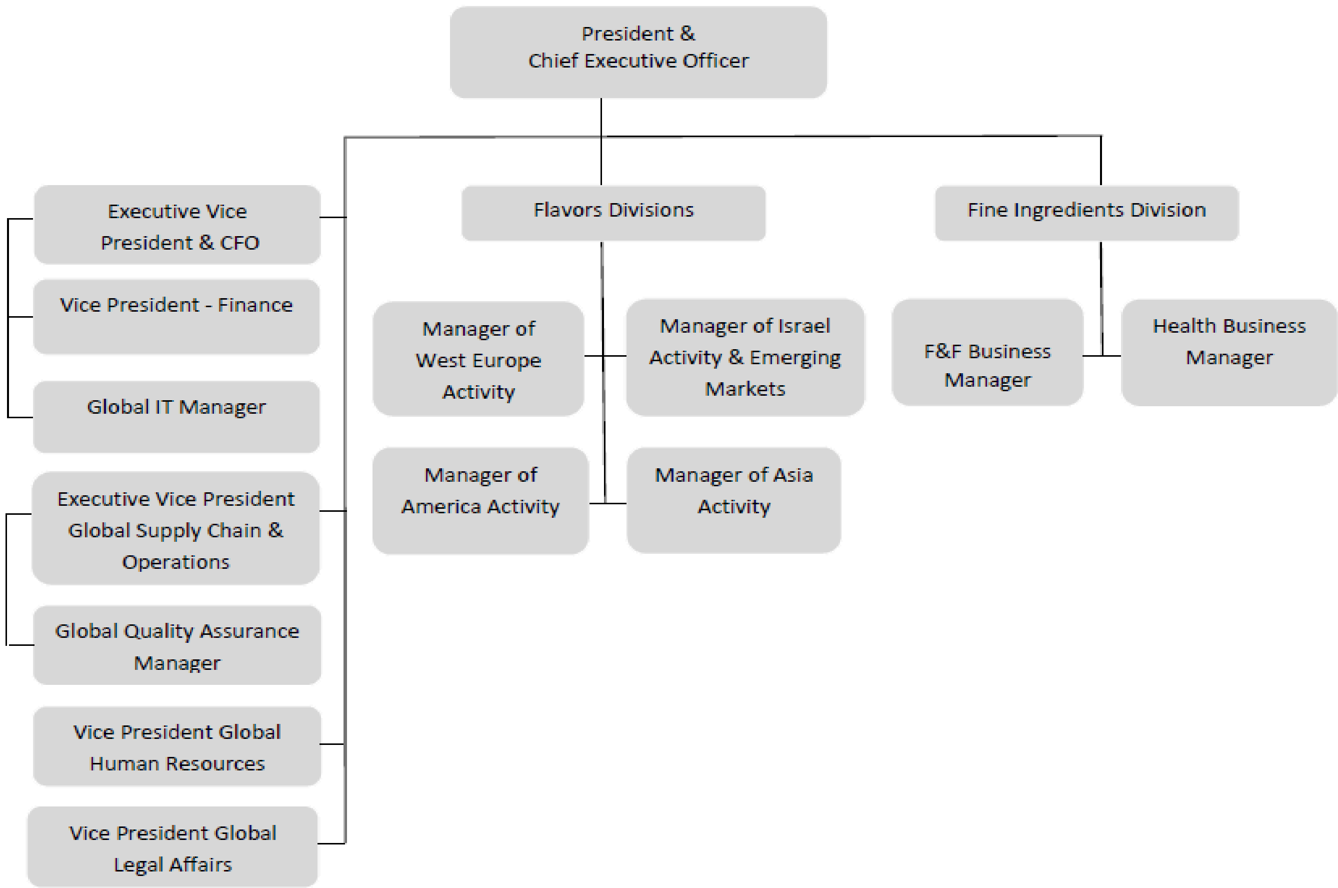
29.1 As at December 31, 2013 Frutarom employs 2,700 employees. The following table shows the number of employees employed by the Group by geographic region over the last two years:

Country	**31.12.2013**	**31.12.2012**
Israel	310	297
Switzerland	187	194
Germany	326	352
UK	298	293
USA	277	207
Belgium	34	32
China and the Far East	199	176
Russia	539	38
Ukraine	12	14
Kazakhstan	11	14
France	10	10
Turkey	26	16
Mexico	3	5
Brazil	74	73
Guatemala	55	-
South Africa	47	11
Italy	34	40
Norway	5	5
Czech Republic	3	2
Slovenia	224	212
Serbia	5	6
Slovakia	5	6
Macedonia	2	2
Poland	14	16
Total	**2,700**	**2,021**

29.2 The following table shows the breakdown of the Group's employees by areas of activity in the last two years:

Area	**31.12.2013**	**31.12.2012**
Sales and marketing	678	391
Research and development	365	280
Operations	1,251	1,016
Management	406	334
Total	**2,700**	**2,021**

29.3 Following is Frutarom's organizational chart:



29.4 The majority of Frutarom's employees at its sites located in Germany, the UK, Slovenia, USA, and Israel (Haifa) are covered by collective bargaining agreements. These agreements vary from country to country and deal principally with conditions of employment, salaries, pension schemes, certain benefit programs, procedures for hiring and dismissing employees and procedures for settling labor disputes.

Employees that are not covered by collective bargaining agreements have personal employment agreements that vary from country to country based on the respective local regulation.

Directors and Senior Management in the Company

29.5 As of December 31, 2013, the Company's senior management included six senior officeholders. In addition, the Group's global management includes five additional managers. The Company has personal employment contracts with the members of the management. These contracts include standard clauses regarding non-competition, confidentiality, and transfer of intellectual property rights to the Company, as is customary in the industry in which the Company operates.

29.6 A number of members of the Company's senior management are entitled to extended advance notice periods ranging between six and twelve months in the case of termination within a period of 12 months from the date on which ICC Handels AG's[18] holdings in the Company's share capital falls below 26%. Furthermore, upon the occurrence of such a change in control, all options and/or ordinary shares previously granted to these members of the senior management will become immediately exercisable, even if they have not yet matured.

29.7 Company director are insured under directors' and office holders' insurance policies. In addition, the Company also granted the officeholders an undertaking for advance indemnification and exculpation for actions taken by virtue of their office in the Company, subject to the restrictions provided by law. For further information see regulation 22 to Chapter 4 to the Company's 2013 Annual Report (Additional Details regarding the Corporation)

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

[18] To the best of the Company's knowledge, ICC Handels AG is fully owned subsidiary of ICC Industries Inc., the Company's controlling party.

30 Employee Incentive Plans

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

31 Raw Materials and Suppliers

31.1 Frutarom purchases thousands of raw materials from a wide range of suppliers which it uses for the manufacture of its products, with more than one supplier for most raw materials. The principal raw materials purchased by Frutarom include plants, leaves and roots from which the Company produces natural flavor extracts, functional food ingredients and pharmaceutical/nutraceutical extracts. In addition the Group purchases essential oils from which it manufactures specialty essential oils such as citrus oils and mint oils. Other raw materials purchased by the Group include natural and synthetic chemicals, alcohol, esters and acids and oleoresins. The Group's supply chain managers, both global and local, and the purchasing units regularly monitor the raw materials price trend and if necessary, the Group acts to adjust the selling prices of its products based on the changes in the raw material prices. Frutarom has a global unit serving both of the Group's primary activities, which supports coordinated the coordination of purchase of strategic raw materials from suppliers,.

31.2 In recent years, none of Frutarom's suppliers have supplied more than 10% of the consumption of its raw materials. There is a small number of raw materials for which Frutarom has sole suppliers; however, since these raw materials are used in only a limited number of Frutarom's products (none of which is substantial) out of wide range of approximately 30,000 products, the Company's management estimates that Frutarom's dependency on these exclusive suppliers is not material.

31.3 Frutarom seeks to reduce costs of raw material used for the manufacture of its products, and to secure constant supply by purchasing raw materials directly from the source, with the aim of expanding its global procurement capacity in source countries, strengthening its global purchase capacity in countries which serve as important sources of many raw materials such as China, India and Brazil, expanding the pool of suppliers and strengthening relations with manufacturers, processors and growers of raw materials. The purchase of the raw materials used for the manufacture of the products of the Group's two business activities is implemented through the support of the global headquarters of the supply chain in order to leverage the purchasing power of the raw materials in large quantities and achieve competitive prices. Frutarom is acting to strengthen and to establish a global purchase system, utilizing its increased purchasing power resulting mainly from its recent acquisitions, which significantly increased the Groups scope of activity.

31.4 The Group carefully manages its global supply chain and acts to strengthen its relations with manufacturers, processors and growers of raw materials, mainly natural raw materials, in order to ensure availability of raw materials at its various production facilities. Frutarom maintains relatively high inventory of certain raw materials, as most of the natural ingredients used by Frutarom in its production are crop- related goods. In addition, raw material delivery times are generally longer than the delivery times to which Frutarom has committed, thereby requiring Frutarom to maintain inventory of raw materials sufficient to enable it to supply its products to customers as ordered with short lead times. However, Frutarom generally maintains comparatively low inventory of finished goods. Furthermore, the availability and the prices of many of the raw materials used by Frutarom to manufacture its products, and in particular the natural ingredients, are subject to fluctuations as a result of international supply and demand. In recent years we have been witness to a continuing trend of a substantial rise in the price of most of the raw materials Frutarom uses to produce its products. 2013 saw stabilization in price levels for most raw materials Frutarom closely monitors any changes in the prices of the raw materials it uses for the manufacture of its products, and when need be, acts to prevent the impact of any increases in prices of raw materials on its activity results, including by adjusting the sale prices of the products impacted by the rise in raw material prices, expanding the supplier pool, and optimizing and maximizing the capacities of Frutarom's production sites throughout the world.

32. Working Capital

Frutarom's working capital is made up of cash and cash equivalents, debtors and debit balance and inventory, less short term credit and loans and current maturities of long term loans, creditors and credit balances. For further information see the Company's balance sheet in its financial reports.

33. Investments

33.1 The Group capital expenditure is primarily the result of the enhancement and expansion of existing facilities, as well as investment in developing new manufacturing facilities, investment in environmental protection, establishment of sales and marketing offices and research and development laboratories.

33.2 The Group's planned investments for the next three years are expected to average between approximately US$20 million to US$24 million per year. Most of the planned capital expenditures in the coming years are related to upgrades of existing production facilities and the improvement of their efficiency, continued implementation of a new company-wide IT system, improvements and capacity increases to Frutarom's production facilities, and investment in ecology, energy conservation and environment. The Group will examine the implementation of the various investments as necessary. The Company has is working towards the establishment of a new plant in China for the production of sweet and savory flavors including sophisticated laboratories for development and applications. Construction at the beginning of 2014, and is expected to be concluded at the beginning of 2015. Over 2012 Frutarom was granted approval by the Ministry of Industry and Trade for the construction of a new plant in Israel, which will expand its research, development and production in Israel and the world, and will serve as a research and development center for natural products. The new plant will be located in Gilboa, a national priority area. An investment grant and tax benefits have been granted under the Israeli Encouragement of Investments Law. The investment grant will be at least 20% of the Company's investment in permanent assets. The plant will be built on 64,000 square meters. The investment in the new plant is expected to be approximately US$30 M.

33.3 The balance of the depreciated cost of the fixed assets in the Company's balance sheet as at December 31, 2013 following deduction of investment grants is US$208.6 million. For further information on the Company's investment in fixed assets see Note 7 to the Financial Reports.

33.4 The Company's management estimates that the cash flow from current operating activities will be sufficient to meet the Company's anticipated capital expenditure and working capital requirements to support the Company's internal growth in the next several years.

34. Financing

34.1 Frutarom's activity is financed through equity and long- and short-term loans from banks. During the period reported, the average and effective interest on the loans were set at 1.57%.

34.2 During 2013 Frutarom used long term loans from banks for the purpose of financing acquisition made over the last few years. As at December 31, 2013, the net debt balance to banks totaled US$190 million. For further information regarding the loan the Group took from banking corporations in 2013, see Notes 9 and 14 to the financial reports.

34.3 After the balance sheet date, on January 23, 2014, the Groups replaced a short term loan it had taken for interim financing of the acquisition of PTI with a three year loan in the amount of FS45.8 million, at LIBOR + 1.4% interest. Interest will be paid every calendar quarter, half the principal to be paid in equal quarterly installments and the balance of the principal to be paid at the end of the loan period. As security, Frutarom Ltd. provided a loan guarantee. There were no changes in the Company's financial covenants, as stated in section 34.4 below

34.4 As part of an update to the credit framework available to the Group, the following financial covenants were updated on February 16, 2012 as follows:

- The Company's equity will not at any time be less than US$300,000 thousand. As of December 2013, the Company's equity stood at US$521.1 thousand.

- The Company's equity will not at any time be less than an amount equal to 35% of the Company's balance sheet. As of December 2013, the Company's equity stood at approximately 53.7% of the Company's total balance sheet.

- The debt ratio after deduction of cash to EBITDA will not exceed 4.25. As of December 31, 2013 the ratio stood at 1.6.

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

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

  1) Up to 50% of the surplus balance accumulated up to December 31, 2011, as this figure appeared in the Company's balance relating to December 31, 2011.

  2) Up to 50% of the Company's annual profits for each calendar year, as this figure appears in the Company's annual financial reports relating to same calendar year in which said profits accrued.

For further details on the liabilities with respect to the above financial covenants, the negative pledge and restrictions on distribution of dividends, and updates, see Note 14 to the Financial Reports and the Company's immediate report dated February 16, 2012.

34.5 In view of Frutarom's solid capital structure, achieved by the support of the strong cash flow generated by Frutarom over the last few years, Frutarom is currently not engaged in contractual credit lines arrangements with banks, and there are no current liens on its assets. The Group has understandings with leading banks worldwide allowing it to finance accelerated growth and strategic acquisitions as necessary.

34.6 The Company's management believes that it will not be required to raise capital in the next year for its ongoing activities.

34.7 For further details on the Company's loans see Note 9 to the Financial Reports.

35. Taxation

35.1 For details of tax regulations applicable to the Company see Note 13 in the Financial Reports.

35.2 The Company has final tax assessments in Israel until 2009, inclusive.

35.3 The Company operates throughout the world, and as of the date of publication of the report, applicable tax rates which apply in various countries in which the Group operates vary from 13% to 42%. For details on the Company's related companies abroad see Note 13 to the Financial Reports.

35.4 The effective tax rate (in the consolidated report) in 2013 was 19.7% compared with 20.8% in 2012. For details on the changes between the Company's statutory tax rate and the effective tax rates see Note 13 to the Financial Reports.

36. Environmental Risk Management

Environmental Hazards

As of the date of publication of this report, Frutarom has 33 plants worldwide which engage in the production of flavors and specialty fine ingredients, using and producing substances considered to be hazardous. These plants are therefore subject to different local legislation and regulations related to the environment and the prevention of environmental hazards.

36.1 Environmental hazards which may materially affect the Group are:

36.1.1 The emission of substances as a result of manufacturing activities at a number of the Company's production facilities, which may harm humans and the environment if emissions are higher than the permitted volumes or concentrations. These hazards include odors which can drift outside the facility and become an odor nuisance, as defined by the relevant local legislation. The Company takes the required steps to prevent uncontrolled emission of such substances according to the provisions of the applicable law.

36.1.2 The Company's production, maintenance and use of materials in a number of the Company's production plants which are defined as hazardous by the applicable local law (mainly flammable substances) may harm humans and the environment if they are not kept under the permitted conditions. The Company holds these substances under in accordance with the provisions of applicable law, and takes the safety measures required when using these substances.

Material Implications of Regulations

36.2 On October 30, 2007, the IPPC directive (96/61/EC) came into effect ("**Directive"**) in the European Union. This Directive sets stringent standards in all matters relating to preventing environmental hazards and is enforced on the Group's sites in Europe.

On January 1, 2008 the Clean Air Law – 2008 ("**Clean Air Law"**) came into effect, adopting the principles of the Directive and applying these to plants defined as "sources of emissions requiring permits". As the Company's plant in Haifa is such "source of emissions requiring 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 emission terms, the Haifa site will have to comply with environmental demands and additional designated fees compared to those which were applicable by law to date.

Material Litigation and Administrative Procedures Relating to the Environment

36.3 During the reported period and until the date of publication of this report, there were no material legal or administrative procedures relating to environment protection pending against the Company or to which an officer of the Company is a party.

The Group's Policy on Environmental Risk Management

36.4 Frutarom has acted and continuously takes action to prevent environmental hazards and to protect the environment. The Company has been authorized within the framework of the Responsible Care program. The Company's management maintains a constant watch on the subject of environment protection and acts to reduce the environmental risks at all of the Group's sites.

As part of the implementation of the Frutarom's strategic program for environmental protection, environmental trustees have been appointed at the Group's key production sites in the world. The trustees have undergone routine validation and training in order to increase the involvement and awareness of the employees at all the Group's sites to the subject of protecting the environment.

All of the Group's sites hold the licenses relevant to the legislative system in their country and, in the Company's assessment, act in accordance with the law.

36.5 Following is a list of the Frutarom Group's key activities for reducing environmental hazards during 2013:

- According to the addendum to the Environmental Arrangement Document agreed upon 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 2013, 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.

Significant Environmental Amounts, Deductions and Costs

36.6 During the reported period and until the date of publication of this report, there were no significant amounts relating to the environments that were awarded against the Company.

36.7 The total amount spent by the Company due to environmental costs in 2013 totaled US$2.2 million. This amount was spent for the prevention and reduction of environmental hazards and does not include investments made by the Company in its facilities as stated above. The Company does not foresee a significant change in the above costs during 2014.

37. Limitations and Supervision of the Company's Business

37.1 The Company develops, produces and markets its products in a number of jurisdictions 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 into local law in the European countries in which the Company operates; and regulations determined by the Ministry of Health in Israel. These laws and regulations determine standards relating to food production, food marking and production facilities, equipment and the personnel required to produce products for human consumption.

37.2 In addition, the Company is 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 various countries which are subject to environmental standards relating to air emissions, sewage discharges, the use of hazardous materials, waste disposal practices and clean-up of existing environmental contamination. In recent years, there has been a significant increase in the stringency of environmental regulation and enforcement of environmental standards throughout the world, and the costs of compliance have risen significantly.

37.3 Frutarom estimates that it currently operates its facilities in compliance with relevant laws and regulations related to food manufacturing, work safety, health and the environment.

37.4 For further information on regulation, health, safety and permits see to section 15.10 of this report.

38. Material Agreements and Cooperation Agreements

For details regarding the Company's commitment to meet certain financial criteria provided by the Company to financing banking institutes to see section 33.4 of this report.

38.1 For details regarding substantial loans the Group has taken from banking corporations, see Note 9 to the Company's financial statements.

38.2 The Company is not a party to strategic cooperation agreements.

39. Legal Proceedings

39.1 For details regarding legal proceedings in which the Company is involved, see section 35.5 above, and Note 11b(2) of the Financial Reports.

39.2 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 reports.

40. Goals and Business Strategy

Frutarom's strategic objective is to achieve growth combining rapid profitable organic growth of its core business, together with strategic acquisitions in order to achieve its vision:

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

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

40.1 **Increasing the Share of the Flavors' Activity**- The successful implementation of Frutarom's rapid and profitable growth strategy allowed Frutarom to significantly increase its Flavors activity, the more profitable of its activities, achieving growth at a higher rate than that of the markets in which it operates. Revenues of the Flavors activity currently form 73% of total Frutarom's revenues compared to 33% in 2000. The Company estimates that the rapid growth trend will continue even under today's challenging market conditions.

40.2 **Development of New Products and Solutions Combining Taste and Health** - Frutarom develops innovative flavor 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 and health give the Company an important competitive advantage among customers in both developed and emerging markets. These new and innovative products are for the main part of higher margins, and therefore contribute not only to a growth in sales but also to Frutarom's improved product mix and profitability.

40.3 **Improvements in Specialty Fine Ingredients Product Mix** – 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 of its margins. Frutarom anticipates continued improved results for the Specialty Fine Ingredients activity also as a result of the successful introduction of new and innovative products that are currently in the pipeline.

40.4 **Strategic Change in the Geographic Mix** - 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, resulted in Frutarom's revenues this year (combined with the acquisitions made this year, had they been consolidated from the beginning of the year) to triple in developing markets, and double in the United States (compared to 2010). At the same time, the Flavors activity in the United States grew by a factor of four. As a result of this massive growth the revenues of Frutarom in Western Europe was reduced from 51% in 2010 to 34% this year.

The five acquisitions made by Frutarom in 2013 and in the beginning of 2014 (JannDeRee in South Africa, PTI in Russia – with sales in additional locations in Eastern Europe, Aroma in Guatemala, Hagelin in the United States -with significant sales in Africa and in Latin America, and the American CitraSource) will all contribute to Frutarom's accelerated growth and to an increase in market share in emerging markets and in the United States in the coming years.

Frutarom focuses and will continue to invest a great deal of resources on accelerating growth and increasing the share of its revenues from emerging markets and the Unites States among other things by focused strengthening of its R&D, production, marketing and sales systems in important target countries and execution of additional strategic acquisitions. At the same time Frutarom continues to expand its activities in the markets of Western Europe, and will continue doing so. The major countries in Western Europe report signs that mark an end to the recession and the slow return to growth, and if this trend continues it will contribute to the improvement of the growth in sales in these important markets.

40.5 **Focus on providing quality service and product development for large multi-national customers and for medium size 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. Frutarom will continue to focus on providing niche value added products to the large multinational food and beverage manufacturers and on expanding its portfolio of natural food solutions. For the 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 dates of delivery.

40.6 **Acquisitions and Mergers, and their contribution to the achievement of 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 in order to leverage the many cross-selling and operational savings opportunities and to 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 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, and in the beginning of 2014 made the further acquisition of the American CitraSource.

Increase in Profit and Profit Margins

40.7 **Contribution and integration of acquisitions** – Integration of the eight acquisitions made in 2011 and 2012 was performed successfully and according to plan, and these acquisitions have already contributed not only to Frutarom's growth in sales but also to the significant improvement in profits this year. Frutarom continues to realize the many cross-selling opportunities and enhanced technological capacities resulting from these acquisitions, and to realize the savings resulting from the integration of R&D, sales, marketing, supply chain, operations and purchasing infrastructures. The full potential of the synergies presented by the acquisitions has not yet been realized, and Frutarom is working to maximize the many benefits from these integrations. Integration of the five acquisitions made in 2013 and in the beginning of 2104 is moving ahead successfully, and these are expected to contribute to Frutarom's continued growth in sales and profit starting already in 2014 and in the coming years.

40.8 **Integration of R&D systems** – Frutarom is working to maximally utilize the many research, development, innovation and technological capacities is has gained over the last few years following the acquisitions, and to implement a new system for managing customers and R&D projects and applications, both on a site level and by connecting between its various R&D sites specializing in the same selection of products. The system will contribute to more focused and efficient management of the R&D efforts across the group and of the development and implementation of the unique solutions for customers, while achieving optimal cross-company solutions and increasing customer satisfaction.

40.9 **Strengthening Global Purchasing** - Frutarom continues to build and strengthen its global purchasing system, leveraging its size following the recent acquisitions, and while 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 capitalizing on the harmonization of the raw materials used in the development and manufacture of all of its products.

40.10 **Operational Efficiencies - Operational Savings** – Frutarom is continually planning, executing and implementing more projects for the unification between and consolidation of production sites, and is striving to achieve efficiency in logistics and supply chain which will contribute to strengthening of its competitive advantage and improve its profit margins over the coming years.

Frutarom expects that the continued execution of its rapid and profitable growth strategy, the continued stabilization of prices of the raw materials it uses in the manufacture of its products and the strengthening of its global purchasing system, together with the contribution of the operational efficiency efforts, improvement of its costs structure, optimal utilization of its productions sites throughout the world and the successfully integrating of recent acquisitions will result in a continuing trend of improved profit and margins and the achievement of Frutarom's revenue target of 1 billion dollars and an EBITDA margin of 20% in the core business.

41. Financial Data Regarding Geographic Regions

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

41.1 The following table sets forth the Company's consolidated income from externals by sales to customer per each customer's geographic regions (in US$ millions):

	2011	**2012**	**2013**	**(%) of total 2013 Sales**
EMEA*	359.2	428.3	471.5	70%
America**	60.3	91.1	93.1	13.8%
Asia & the Far East	55.0	57.5	66.5	9.9%
Israel***	43.9	41.1	42.6	6.3%
Total	518.4	618.0	673.7	100%

* **"EMEA"** in this report is defined as: Europe, Africa and the Middle East (excluding Israel).

Sales in Germany reached US$84.2 million, US$74.1 and US$71.9 million in 2011, 2012 and 2013, respectively. .

** In this report, America includes sales in the US in the sum of US$66.8 million, US$63.9 million and US$45.2 million in 2013, 2012 and 2011, respectively.

41.2 Data according to geographic regions of main production sites:

41.2.1 Following is the sales breakdown as per geographic locations of main production sites:

	2013 in US$ Thousands				2012 in US$ Thousands				2011 in US$ Thousands			
	Flavors	Raw Materials	Cancel-lations	Total	Flavors	Raw Materials	Cancel-lations	Total	Flavors	Raw Materials	Cancel-lations	Total
Europe	367,725	57,056	(2,255)	422,526	338,907	57,840	(1,020)	395,727	273,240	60,689	(408)	333,520
America	44,001	27,066	-	71,067	40,050	27,719	-	67,769	19,683	26,465	-	46,148
Israel	46,650	37,742	(1,146)	83,246	46,399	33,587	(1,083)	78,903	50,062	35,857	(1,640)	84,279

*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.

41.2.2 Following is the breakdown of operating profit by the geographic regions of main production sites and activities:

Flavor Activity	2013	2012	2011
% operating profit	13.9%	13.0%	12.7%
Europe	14.4%	14.0%	13.1%
America	19.1%	18.0%	15.0%
Israel	23.9%	19.8%	20.6%

Specialty Fine Ingredients Activity	2013	2012	2011
% operating profit	11.8%	8.8%	8.1%
Europe	13.3%	8.4%	7.9%
America	3.4%	3.4%	5.1%
Israel	22.5%	13.4%	16.5%

41.2.3 Total assets (without intercompany balances) by geographic locations of main production sites in US$ thousands:

	2013	2012	2011
Europe	540,084	459,503	370,719
America	167,131	113,240	114,260
Israel	71,811	67,435	74,944

41.3 For further information regarding geographic regions see Note (6) of the Financial Reports.

42. Risk Factors

Below are the main risk factors:

Macroeconomic Risks

- **The effects 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 a decrease in demand for the Company's products (mainly for premium products) and significantly slow down the development and launch of new products by Frutarom's customers. A global financial crisis could harm Frutarom's ability to raise funds required for the execution of its strategic acquisitions. Over the last few years we have been witness to financial uncertainty in world markets, especially in Europe, including in some EU member countries, in which significant financial crisis has even caused a recession.

- **Stability in emerging markets**

  Frutarom operates in a number of countries outside of Western Europe and the United States, such as Russia, Ukraine, Turkey, Slovenia, Kazakhstan, China, countries in South and Central America (Brazil, Guatemala and Mexico) and countries in North, South and West Africa, and therefore Frutarom is exposed to the political, economic and legal systems and conditions 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 or the expropriation and/or nationalization of its assets situated there. There is also a significant risk relating to operations in emerging market countries arising from the establishment or enforcement of foreign exchange restrictions, which could effectively prevent Frutarom's ability to fully realize its profits, or sell its assets in these countries. While none of the emerging market countries in which Frutarom operates currently have foreign exchange controls that affect it significantly, many of these countries have had such controls in the recent past and there is no certainty that such controls will not be reinstituted in the future.

- **Currency fluctuations**

  For details regarding the risks from currency fluctuations, see currency risks in chapter B, Exposure to Market Risks and Risk

Management in the Board of Directors' Report, and Note 3A to the financial reports.

- **Changes in interest rates**

For details regarding the risks from changes in interest rates, see interest rate risks in chapter B, Exposure to Market Risks and Risk Management in the Board of Directors' Report and Note 3A to the financial reports.

<u>Industry Related Risks</u>

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

Frutarom faces competition both from large multinational and mid-sized companies as well as smaller 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 systems and more established reputations, 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 with regard to large multinationals. Furthermore, large multinationals, and increasingly, mid-sized customers, limit the number of their suppliers, working only with a limited list of "approved suppliers". To compete more successfully in this environment, Frutarom must make greater investments in customer relationships and tailored product research and development in order to anticipate customers' needs and to provide effective service. A failure by the Group to maintain its good relations with its existing customers, establish good relations with new customers, or secure inclusion on certain of the "approved suppliers" lists of some customers, could have a material adverse effect on its business, results of operations or financial condition.

In comparison to the flavor market, the fine ingredients market is more price sensitive and is characterized by comparatively lower margins. Some of the fine ingredients products, manufactured by the Company, are less specialized and more interchangeable with those of its competitors. In addition, overcapacity in the global production of certain types of fine ingredients may have a negative impact on Frutarom's sales and profitability. Although Frutarom is focusing as part of its strategy on those fine ingredients products exhibiting higher margins, there can be no certainty that operating profits margins for its fine ingredients products will not decrease in the future, which could in turn have a material adverse effect on the Group’s business, results of operations or financial condition.

- **The effect of changes in regulations on the Group**

  Frutarom is subject to a variety of health, safety and environmental rules at international, 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 general public awareness regarding the composition and use of flavor products and from the fact that as a result of their medicinal qualities and claimed health benefits, nutraceuticals 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. Frutarom has identified nutraceuticals and functional food ingredients as important markets for its future growth. The application of new regulations on these markets could result in substantially greater ongoing compliance costs, which, in turn, could have a material adverse effect on the Company’s business, results of operations or financial condition.

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

  Companies operating in the flavor and fine ingredients industry, such as Frutarom, also use, manufacture, sell and distribute a number of hazardous substances, and therefore are subject to extensive regulation regarding the storage, handling, manufacture, transportation, use and disposal of such substances, their ingredients and byproducts. This is particularly relevant for Frutarom’s production and research and development activities in the UK, Switzerland, Germany, Italy, the US, Israel, Russia, Slovenia, China, Brazil, Guatemala and other countries in which the business operations are subject to laws, regulations and standards relating to air emissions, sewage discharges, the use, handling and discharge of hazardous materials, waste disposal practices and clean-up of existing environmental contamination. Any increase in the stringency of such laws and regulations could have a material adverse effect on the Group's business, results of operations or financial condition.

  In addition to ongoing environmental compliance costs, the Company might, from time to time, be required to incur extraordinary one-time expenditures to meet applicable environmental regulations and standards and may be liable for costs associated with any remedial actions that are required in locations in which the Company’s facilities are located. As the

Company cannot predict such environmental events with certainty, the amounts the Company has budgeted or will budget in the future may not be adequate. Both the ongoing costs of and non-recurring expenditures relating to such may have a material adverse effect on the Company's business, results of operations or financial condition.

Frutarom is required to maintain and hold various environmental permits for operations at its facilities and is required to conduct its operations in accordance with conditions specified in these permits. Plant expansions are also subject to the securing of necessary permits. All such permits may be revoked or modified by the relevant regulator acting unilaterally, and certain permits are time-limited and require periodic renewal. Any such revocation, modification and/or failure to renew a permit could have a material adverse effect on the Company's business, results of operations or financial condition.

- **Exposure to civil and criminal liabilities in connection with environmental, health and safety laws and regulations applicable to the Group**

The environmental, health and safety laws and regulations, may impose on Frutarom significant civil and criminal liabilities for environmental pollution as well as for non-compliance with applicable laws, regulations and standards. Environmental and health and safety laws may include criminal sanctions (including substantial penalties) for violations of such laws and regulations. Some environmental laws also provide for strict liability for releases of hazardous substances, which could result in the Company being liable for remedying environmental damage without regard to its negligence or fault. Other environmental laws impose joint and several liability for the clean-up of pollution and contamination and could therefore expose the Group to liability arising out of the conduct of others.

In addition, some environmental, health and safety laws may apply retroactively, imposing liability for past actions even when such though those actions were implemented in compliance with all applicable laws at the relevant time. Any civil or criminal liability under these laws may adversely affect the Company's business, results of operations or financial condition.

Additionally, Frutarom may be subject to claims alleging personal injury or property damage as a result of alleged exposure to hazardous substances. The laws in the principal countries in which the Group operates allow for legal proceedings to be taken against it if its production facilities are alleged to have caused environmental contamination or personal injury. These proceedings may also be taken by either private individuals or by non-governmental organizations.

- **Fluctuations in prices of raw materials required for the production of the Group's products**

  For details regarding the risks from fluctuations in prices of raw materials required for production of Frutarom products, see the description of market risks in the Exposure to Market Risks and Risk Management in the Board of Directors' Report.

- **Dependency on suppliers of unique raw materials and availability of natural ingredients**

  Frutarom is dependent on third parties for the supply of raw materials it requires to manufacture its products. Although the Group purchases raw materials from a very wide range of suppliers, with no single supplier representing more than 10% of its total raw material purchases by the Group, there can be no guarantee that this will continue to be the case. Significant weather damages may cause a material shortage in natural ingredients which the Company uses. A shortage in these raw materials can damage Frutarom's sales for a certain period of time.

- **Payment of damages as a result of possible product liability claims due to product warranty**

  The Company's business exposes it to a risk of product liability, particularly as it is involved in the supply of flavors and fine ingredients to the food and beverage, flavor and fragrance, functional food, pharmaceutical/ nutraceutical and personal care industries. If a large product liability claim was successfully brought against the Company, its insurance coverage might not be adequate or sufficient to cover such a claim in terms of paying damages and/or defense costs. A lack of or inadequate insurance coverage could result in a material adverse effect on the Company's business, results of operations or financial condition. If product liability claims were brought against the Company, it might damage the Company's reputation as well as require the Company to divert significant time and effort of its management, which could adversely affect the Company's business regardless of the outcome of the claim.

Risk Factors Unique to the Group

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

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

  Merging 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 attention, failure to retain key personnel, risks associated with unanticipated events in the integration of the operations, technologies, systems, services and products of the acquired businesses. In addition, Frutarom may be unable to achieve the anticipated synergies (including those aimed at cost savings) from such acquisitions. Any failure to successfully integrate past or future acquisitions could have a material adverse effect on the Company's business, results of operations or financial condition.

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

  The rapid growth, in both operations and geographical spread as was in recent years, requires effective management to ensure that the expected financial benefits through synergies and economies of scale are realized. An inability to adapt effectively to the rapid growth could result in losses or acquisition costs for Frutarom, such that are not recovered as quickly as anticipated, if at all. Such problems could have a material adverse effect on the Company's business, results of operations or financial condition.

- **Employing and retaining key employees**

  The Company's continued success depends on its ability to attract and retain trained flavorists, laboratory technicians and other skilled personnel. The Company operates in a highly specialized market where the quality of product is crucial and skilled personnel are critical to ensuring the delivery of a high quality products. If a number of such employees were to leave simultaneously the Company could have difficulty locating replacement personnel with the same experience and skill, in which case the Group's research and development capabilities could be impacted. Further, Frutarom’s continued success depends to a large extent on its senior management team. The loss of the services of certain members of its 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 attract and retain trained personnel or members of senior management could have a material adverse effect on the Company’s business, results of operations or financial condition.

- **Protection of intellectual property**

The Group’s business depends on intellectual property, which consists mainly of formulas used to create its flavors. Frutarom’s formulas are not registered as patents but constitute highly confidential proprietary business information, available to very few people even within the Group. Although Frutarom believes that it is not depends materially on any single proprietary formula, license or other intellectual property right, the loss of confidentiality with respect to proprietary formulas or loss of access to them and/or the future expiration of intellectual property rights could have an adverse impact on the Group’s business, results of operations or financial condition.

Frutarom relies, in part, on confidentiality 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 Frutarom may not have adequate remedies for any such breach. Disputes may arise concerning the ownership of intellectual property or the applicability of confidentiality agreements. Furthermore, the Company’s trade secrets may become known or independently developed by its competitors in which case the Company may not be able to enjoy exclusively use of some of its formulas or maintain the confidentiality of information relating to its products.

Following is a table that summarizes the various risk factors and the Company's evaluation of their level of impact thereon:

Risk Factor	Risk factor's level of impact on the Company		
	High	Medium	Low
Macroeconomic Risks			
Effects of the global economy		√	
Stability in emerging markets		√	
Currency fluctuations		√	
Changes in interest rates		√	
Industry Related Risks			
Competition in the markets		√	
Changes in regulations		√	
Compliance with standards		√	
Exposures to liabilities		√	
Fluctuations in prices of raw materials		√	
Dependency on suppliers of unique raw materials and availability of		√	
Product liability claims		√	
Risks Unique to the Company's Business			
Identification of future acquisitions		√	
Adaptation to rapid growth		√	
Attraction and retention of key employees			√
Protection of intellectual property			√

43. Details about valuations

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

Valuation subject	Goodwill of the savory activity (Germany, Norway, Italy)
Valuator	BDO Ziv Haft Consultants and Management Ltd.
Valuation requester	Frutarom Industries Ltd., by Mr. Guy Gill, VP Finance
Engagement date	December 2013
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, 2013. Valuation was conducted during March 2014.
Value of goodwill prior to valuation date	€150,246 thousand
Value of goodwill according to valuation	€142,072 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: Pini Shmueli Nissan.

	Evaluator's education • BA in Economics, Ben Gurion University of the Negev. • M.Sc. in economics, Eitan Bargelis School at the Tel-Aviv University. Positions held: • Director of research and consulting department at Forsyth; • Director of consulting department at Ernst & Young Areas of 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	• Capitalization rate: 15.7% before taxes • Growth rate: 2% long term • Sensitivity to growth: 1% through 3% • Sensitivity of capitalization rate: 13.7%-17.7% Data used as a basis for comparison: the activity's results in recent years and its forecast.
Prior Valuation	• Valuation dated December 31, 2012 conducted by Ziv Haft Consultants and Management Ltd., signed on March 11, 2013. Value of activity according to the above valuation was €150,246 thousand.

43.2. Details about the valuation for the Flavors Activity in in the United States in accordance with Accounting Regulation 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 2013
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, 2013. Valuation was conducted during March 2014.
Value of goodwill prior to valuation date	US$92.247 thousand
Value of goodwill according to valuation	US$102,743 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: Pini Shmueli Nissan. Evaluator's education • BA in Economics, Ben Gurion University of the Negev.

	• M.Sc in economics, Eitan Bargelis School at the Tel-Aviv University. Positions held: • Director of research and consulting department at Forsyth; • Director of consulting department at Ernst & Young Areas of 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	• Capitalization rate: 15% before taxes • Growth rate: 2% long term • Sensitivity to growth: 1% through 3% • Sensitivity of capitalization rate: 16%-18% Data used as a basis for comparison: the activity's results in recent years and its forecast.

IMPAIRMENT STUDY
SAVORY UNIT

Frutarom Industries Ltd.

Impairment Study - Savory Unit
As Of December, 2013

March 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 Savory sector (Hereinafter: the "**sector**" 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.

The Study was prepared for Frutarom and its management for the purpose of reporting its financial statements as of December 31, 2013, and may be provided to their external auditors. Unless required by applicable law (for instance, reference to a performance of an impairment test and its implications in the financial statements), it is not to be used or quoted in a prospectus and/or any other document without receiving our prior written consent.

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

The following table displays the Unit's revocable amount compared to the carrying amount (thousands €):

€000	2013
Recoverable amount	142,072
Carrying amount	119,881
Impairment amount	-

Source: BDO analysis.

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.

The principal sources of information used in performing our Annual Goodwill Impairment Test include:

- The Unit's unaudited consolidated income statements and balance sheets breakdown for the fiscal year ended 2013, which are based on audited financial statements of the companies comprising the Unit;
- The Unit's annual financial forecast for the years 2014-2019 (Hereinafter: the : "Financial Forecast");
- Other information provided by Management, written or oral;
- Publicly available data;
- Discussions with Management;
- Publicly available information (articles, websites) regarding the industry; and
- Bloomberg and other relevant financial websites.

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.

Respectfully submitted,

BDO Ziv Haft

Consulting & Management Ltd.

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Section 1
Unit Overview

Unit 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.

Acquisitions Agreements

The following description shows the Unit's acquisitions executed by the Company:

- In January 2006, Frutarom acquired 70% of the issued and paid up share equity of GewurzMuhle Nesse GmbH and GewurzMuhle Nesse Gebr. Krause GmbH. The acquisition was performed through Frutarom Germany GmbH, a wholly owned

Acquisitions Agreements

subsidiary of Frutarom. Frutarom paid Euro 18.41 million for the acquisition. During Q1 2008, an additional amount of Euro 18.89 million was paid for the exercise of an option for the acquisition of the remaining 30% of the issued and paid up share capital of Nesse and for the improvement in Nesse's operating profit during the years 2005-2007. As for today, the Company holds 100% of Nesse's share capital. The total purchase price amounted to 38 € million.

The acquisition of Nesse and the exercise of the option were another significant milestone in implementing Frutarom's rapid growth strategy. The acquisition and the exercise of the option strengthened Frutarom's technological capabilities and offering to customers in the savory field and contributed to strengthening and positioning Frutarom as a leading flavours supplier in Western and Eastern Europe. The Nesse acquisition expanded Frutarom's geographic spread to additional countries in which Frutarom was less active, such as Poland, Czech Republic, and Latvia etc.

Nesse's savory activity is synergetic to Frutarom's activities in some of the countries in which it operates, especially in Europe. Frutarom is taking advantage of its large, dedicated global sales and marketing infrastructure to realize the substantial cross-selling opportunities created by the acquisition, by expanding both the customer base and the product portfolio.

- In October 2007, Frutarom acquired 100% of the share capital of Gewurzmuller Group for a cash consideration of 47.3 € million. The acquisition agreement

Unit Overview

Acquisitions Agreements

determined a future payment mechanism so that the final payment to be made will reflect the Gewurzmuller Group's value based on an average EBITDA multiple of 7.1, that the Gewurzmuller Group will achieve during the twelve months ending December 31, 2007.

During the third quarter of 2008, Frutarom paid the remaining said consideration for the acquisition of the Gewurzmuller Group for an amount of approximately 21.7 $ million (approximately Euro 13.9 million). During 2010, Frutarom acted to merge and consolidate the activities of Nesse, the Gewurzmuller Group and the Savory activities of CH for the purpose of achieving maximum efficiency and operational saving. The acquisition considerably boosted both Frutarom's technological capabilities and its product offering to its customers worldwide in the field of savory flavors and functional products, as well as Frutarom's extensive global customer base.

- In June 18, 2009, Frutarom signed, via its subsidiaries in Germany, an agreement to acquire CH's assets and Savory activities (Hereinafter: the "**CH activity**") in consideration of a cash payment of approximately 7.3 $ million (Euro 5.3 million). CH's Savory activity develops, manufactures and markets unique and innovative Savory flavor solutions which include flavors, seasoning mixes and functional raw materials to the food industry with a special emphasis on the processed meat field and convenience food. The activity is highly synergetic to those of the German Nesse and Gewurzmuller Group which were acquired by Frutarom in 2006 and 2007, respectively. During 2009, Frutarom acted to merge and consolidate the

Acquisitions Agreements

activities of Nesse, the Gewurzmuller Group and CH activity for the purpose of achieving maximum efficiency and operational saving.

- On December 23, 2010, Frutarom signed an agreement, via a Norwegian subsidiary, for the acquisition of Rieber's Savory activity (the **"Rieber activity"**) in consideration of approximately 4.3 $ M (approximately NOK 25 M). The acquisition was completed on February 1, 2011.

The Rieber Activity acquired assets include the development, production and marketing of non-sweet flavor solutions including flavors, seasoning mixes and functional ingredients used by the food industry, and in particular by processed meat and fish and convenience food manufacturers. The Rieber Activity includes a research and development and marketing site in Norway as well as a broad customer base including a number of leading food manufacturers located mainly in Scandinavian countries. The Rieber Activity is highly synergetic with Frutarom's savory activity in Europe and in Israel.

During 2011, Frutarom began implementing a plan to transfer production from Norway to Germany. In light of the move, which was successfully completed on November 1, 2011, Germany will produce for Norway the products which Norway will market, utilizing existing knowledge and experience in Germany. This will lead to efficiency and operational savings resulting improvement in earnings and profitability by creating economies of scale for all the Savory activity ("the activity").

Unit Overview

Acquisitions Agreements

- On May 26, 2011, Frutarom signed an agreement, through a subsidiary, for acquisition of the activity and assets of the Christian Hansen Italia (Hereinafter: "**CH Italia activity**") for a consideration of approximately €24 million (approximately $35.7 million). The transaction was financed through short-term bank credit, which was replaced by a loan for 42 months interest rate LIBOR + 2.4%. The acquisition was completed on July 29, 2011. CH Italia Activity's sales turnover during the fiscal year 2010 totalled approximately Euro 18.3 million (approximately $24.3 million).

  CH's Italia activity is synergetic with Frutarom's savory activity and will allow Frutarom to further position itself as a leading company within the European flavour market. Frutarom merged the operation, development and sales activities of CH Italia with its existing activity.

Production Facilities

The following are the main production facilities of the Unit:

- **Nesse-Loxstedt, Germany** (**Nesse**) - At this plant the Company's flavor activity produced savory flavor mixes. This production site was closed July 2013 and production activities were transferred to other plants in Germany and Italy. Frutarom estimates operational efficiency will increase considerably as a result of the closure, particularly regarding personnel and freight costs.

  Production Capacity and Shifts - The plant operates five days a week in one shift. The plant has additional potential production capacity of about 30%-35%, assuming that it shifts to continuous production over three shifts.

- **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.

  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.

Unit Overview

Production Facilities

- **Stuttgart, Germany (Blessing) -** At this plant under the Company's flavor activity, starter cultures are produced (for details regarding starter culture products, refer to section 1.23 of this report).

  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%.

- **Parma, Italy –** this plant was acquired in 2011.

Selling and marketing

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

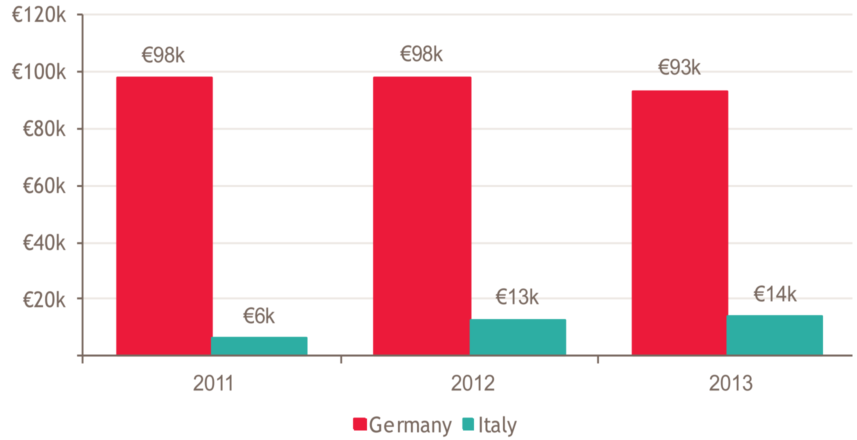
Germany - The German subsidiary has 20 local marketing points and sells units in 20 countries besides Germany, mainly in East and west Europe.

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.

Sales by production site

The following chart presents sales by production site for 2013:



Source: Management information

Unit Overview

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. As is customary in the flavor market, there are no long-term supply contracts.

The German activity's main customers are leading food producers in both East and West Europe especially in Germany, Austria, Switzerland, Sweden, Denmark, Russia, Ukraine and Bulgaria. The CH activity's customers are all over Europe while the River's activity customers are mainly in the Scandinavia countries.

The activity of the Italian CH is market to customers located throughout Europe, while Rieber markets its products primarily in Scandinavia.

Unit Overview

Balance Sheet

The following table presents the unaudited (see source below) balance sheet of the Unit as of December 31, 2012 and 2013 (Thousands €):

€000	2012	2013
Current Assets		
Cash & cash equivalents	7,255	6,552
Accounts receivable	13,536	14,792
Other receivable	1,245	338
Inventory	15,891	16,663
Deferred tax asset	1,272	1,870
Total current assets	39,199	40,214
Net fixed assets	18,296	17,270
Net intangible assets	96,967	93,570
Long term inter-company balances	9,660	-
Total assets	**164,122**	**151,054**
Current liabilities		
Accounts payable	8,664	9,583
Other short-term liabilities	5,007	5,821
Other payables, related parties	2,450	-
Total current liabilities	16,121	15,404
Long term liabilities		
Inter Company loans	31,844	22,090
Pension liability	2,342	2,842
Deferred tax (PPA)	4,766	4,506
Total long term liabilities	**38,952**	**29,438**
Total liabilities	**55,072**	**44,841**
Total shareholder's equity	109,050	106,213
Total liabilities and equity	**164,122**	**151,054**

Source: Management information (unaudited consolidated financial statements for 31 December 2013, 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, 2011, 2012 and 2013 (Thousands €):

€000	2011	2012	2013
Revenue	104,058	111,119	107,436
Growth rate	*na*	*6.8%*	*-3.3%*
Cost of sales	69,504	75,377	71,505
% of revenue	*66.8%*	*67.8%*	*66.6%*
Gross profit	**34,554**	**35,742**	**35,931**
Gross margin	*33.2%*	*32.2%*	*33.4%*
Operating expenses			
R&D	3,350	3,570	4,356
% of revenue	*3.2%*	*3.2%*	*4.1%*
S&M	12,912	14,180	12,874
% of revenue	*12.4%*	*12.8%*	*12.0%*
G&A	4,976	6,854	6,292
% of revenue	*4.8%*	*6.2%*	*5.9%*
Total operating expenses	21,238	24,604	23,522
% of revenue	*20.4%*	*22.1%*	*21.9%*
Operating profit	**13,316**	**11,138**	**12,409**
Operating margin	*12.8%*	*10.0%*	*11.6%*

Source: Management information (unaudited consolidated financial statements for 31 December 2013, 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 2011, 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 18.2 $ billion. According to Leffingwell & Associates, Frutarom is ranked as one of the ten largest companies in the field of taste and smell.

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 3% to 3.4%, from 2013 to 2015. Frutarom estimates that sales of raw materials, in those markets, will grow at an annual rate, similar to the years 2013 to 2015. 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 between 4% and 7.1% from 2013 to 2015.

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.

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

Flavor and fragrance industry worldwide

61% 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 700 such companies that, according to the estimation of Leffingwell & Associates, represent approximately 21% 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 19% 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 2011 sales of flavors for the industry amounted to approximately US $ 8 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. 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.

Market Overview

Flavors market

The following table sets forth the sales of flavors by region in 2011 and the projected annual growth rate in these geographic regions:

Country	Estimated world consumption in 2011 (US$ million)	Average growth expected in 2011-2015
Western Europe	1,668	3.0%
Eastern Europe	573	4.0%
North America	2,394	3.4%
South America	528	7.1%
Asia - Pacific	2,554	5.8%
Middle East and Africa	565	4.4%
Total	**8,282**	**4.5%**

Flavors market

In 2011, Flavors in North America and Western Europe accounted for approximately 50% of global Flavor sales, although the population in these countries account for less than 10% of the world's population.

The demand for Flavor products in developed countries is expected to grow moderately, with more rapid growth expected in emerging markets such as Asia, Central and South America, Eastern Europe and Africa. Sales in these emerging markets are expected to grow as a result of projected growth in GNP in these regions and from changes in consumer preferences.

Frutarom is enhancing its growth in these markets through a number of efforts including a focused strengthening of the research and development, production, marketing and sales infrastructure in the important target countries and exploring options for strategic acquisitions.

Market Overview

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.

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.

Market Overview

Food and Beverage 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 4,486 $ billion in 2011. 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.

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.

Market Overview

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.

  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.

Food and Beverage Market - Tendencies

- **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.

- **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.

Market Overview

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.

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.

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.

Market Overview

Competition

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.

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.

Risks Factors - Macroeconomic Risks

- **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

- **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.

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

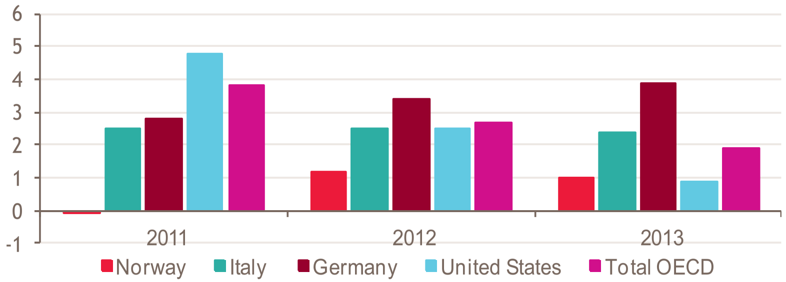
- **Environmental, health and safety regulations** - Companies in the flavor and fine ingredients industry also use, manufacture, sell and distribute a number of environmentally hazardous materials, and therefore are subject to extensive regulation regarding the storage, handling, manufacture, transportation, 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 2010-2013:



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.

Step A – 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.

Step B - Deriving the Recoverable amount

The Recoverable amount will be the higher of values between the Fair value less costs to sell and the Value in use.

Step C - Recognizing and Measuring an Impairment Loss

As mentioned in step B, the recoverable amount will be the higher of values between the Fair value less costs to sell and the Value in use. An entity shall depreciate the value of an Asset or a Cash-generating unit if, and only if, the Recoverable amount of the Asset or the Cash-generating unit is lower than its respective Carrying amount.

In order to determine the need for impairment, this study was prepared using Value in use approach.

Applying IAS 36 - Goodwill

IAS 36 - Long Lived Assets

The Long Lived Assets of the Company, according to the Company's assessments following the acquisition, include Savory Unit's Goodwill.

IAS 36 - Goodwill

To perform the impairment examination we have evaluated the value in use of net assets of the Unit, as of December 31, 2013 by using the discounted cash flow (**DCF**) method under the income approach.

Section 4
DCF Approach

DCF Approach

Revenues

The following table presents the Unit's estimated revenues according to our forecast and the actual revenue results, for the years 2012-2013 (thousands €)

€000	2012	2013	2014	2015	2016	2017	2018	Terminal
Revenue	111,119	107,436	112,808	117,320	121,426	125,069	128,196	130,760
Growth rate	*6.8%*	*-3.3%*	*5.0%*	*4.0%*	*3.5%*	*3.0%*	*2.5%*	*2.0%*

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, 87% of the total Unit's revenue for 2013.
- The savory activity in Italy, 13% of the total Unit's revenue for 2013.

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 2012 the Unit's revenue was c.111 million Euro, an increase of 6.8% from 2011. During 2013 the Unit's revenue was c.107 million Euro, a decrease of 3.3% from 2012.

According to Management, the decrease in revenue during 2013 was driven by low demand in Eastern Europe and the increased focus on the operational efficiency process (closing of the Nesse production site, as mentioned above). Never the less, in light of operational efficiency implementation, gross profit has increased in 2013 and pre tax operational profit increased by 1.3 million Euros from 2012 to 2013.

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 5% 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 natural 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 5% in 2014, to a rate of 2% in the terminal year, representing the long-term growth rate of the Company.

DCF Approach

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 2012-2013 (thousands €):

€000	2012	2013	2014	2015	2016	2017	2018	Terminal
Cost of sales	75,377	71,505	73,915	76,141	78,167	79,964	81,506	82,771
% of revenue	*67.8%*	*66.6%*	*65.5%*	*64.9%*	*64.4%*	*63.9%*	*63.6%*	*63.3%*

Source: Source: BDO analysis and Management's projections

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

In 2012, the cost of sales amounted to 75 million Euros, representing about 67.8% of the total revenues. In 2013, these expenses were a total of c.71.5 million Euros, representing about 66.6% of total revenues.

The process performed to increase operational efficiency (described above) includes closure of the Nesse manufacturing site, transfer of production to other sites in Germany and Italy, organisational restructuring and achieving improved terms of trade with suppliers.

In light of the above, we have projected the total cost of sales in 2014 will decrease to 65.5% of revenue and will reach a level of c.64% in 2017 and up to 63% 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.

Gross profit

The following table presents the Unit's estimated gross profit for 2014-2019 according to our forecast, and the actual gross profit results, for the years 2012-2013 (thousands €):

€000	2012	2013	2014	2015	2016	2017	2018	Terminal
Gross profit	35,742	35,931	38,893	41,179	43,259	45,105	46,690	47,989
Gross margin	*32.2%*	*33.4%*	*34.5%*	*35.1%*	*35.6%*	*36.1%*	*36.4%*	*36.7%*

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 35% in 2014 up to about 37% in the terminal year.

DCF Approach

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 2012-2013 (thousands €):

€000	2012	2013	2014	2015	2016	2017	2018	Terminal
S&M	14,180	12,874	13,228	13,600	13,971	14,319	14,629	14,895
% of revenue	*12.8%*	*12.0%*	*11.7%*	*11.6%*	*11.5%*	*11.4%*	*11.4%*	*11.4%*

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 2012, S&M expenses of the Unit totaled around 14 million Euros, representing about 13% of total revenues. In 2013, these expenses were a total of c.13 million Euros, representing 12% of total revenues. The decrease in S&M expenses was driven by the operational efficiency procedures implemented and improved terms of trade with freight suppliers (according to Management full impact is to be achieved in 2014).

In 2014, according to Management's forecast, it was assumed that sales and marketing expenses will be about 13.2 million Euros and will be about 12% 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.

It was assumed in the long term S&M cost will increase according to the permanent growth rate. Accordingly, the average S&M expenses ratio will decrease gradually to 11.5% in the forecast years and reach c.15 million Euros in the Terminal year.

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 2012-2013 (thousands €):

€000	2012	2013	2014	2015	2016	2017	2018	Terminal
G&A	6,854	6,292	6,403	6,496	6,581	6,657	6,721	6,775
% of revenue	*6.2%*	*5.9%*	*5.7%*	*5.5%*	*5.4%*	*5.3%*	*5.2%*	*5.2%*

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 2012, the G&A expenses were c.6.9 million Euros, which reflect a rate of 6.2% of revenues. In 2013, the G&A expenses were about 6.3 million Euros, which reflect a rate of 5.9% of revenues, with improvement deriving from operational efficiency procedures implemented.

In 2014 Management expects a decrease in G&A costs, as a result of the operational efficiency procedures mentioned above. Accordingly, it was assumed the decrease trend will continue and G&A expenses will be c.6.4 million Euros, c. 5.7% of revenue,

In the forecast years it was assumed G&A expenses as a percentage of revenue will improve gradually to 5.2% of revenue. It was assumed in the long term G&A cost will increase according to the permanent growth rate.

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DCF Approach

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 2012-2013 (thousands €):

€000	2012	2013	2014	2015	2016	2017	2018	Terminal
R&D	3,570	4,356	4,483	4,590	4,687	4,773	4,847	4,908
% of revenue	*3.2%*	*4.1%*	*4.0%*	*3.9%*	*3.9%*	*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 2012, the R&D expenses were 3.6 million Euros, which reflect a rate of 3.2% out of revenues. In 2013, the R&D expenses were 4.4 million Euros, which reflect a rate of c.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 2014, it was assumed R&D expense will be 4.4 million Euros, 4% of revenue, similar to 2013 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.

Operating Profit

The following table presents the Unit's estimated operating profit according to our forecast, and the actual operating profit, for the years 2012-2013 (thousands €):

€000	2012	2013	2014	2015	2016	2017	2018	Terminal
Operating profit	11,138	12,409	14,779	16,493	18,020	19,357	20,492	21,412
Operating margin	*10.0%*	*11.6%*	*13.1%*	*14.1%*	*14.8%*	*15.5%*	*16.0%*	*16.4%*

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 13% in 2014, to 16.4% in the terminal year.

DCF Approach

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 2012-2013 (thousands €):

€000	2012	2013	2014	2015	2016	2017	2018	Terminal
Depreciation	2,977	2,925	2,940	2,953	2,965	2,976	2,985	2,994
Capital expenditure	(900)	(1,600)	(1,470)	(1,772)	(2,075)	(2,380)	(2,687)	(2,994)

Source: BDO analysis and Management's projections

Depreciation expenses were c.3 million Euros in 2013. In order to forecast the depreciation expense projections it was assumed depreciation expense will increase slightly up to c.3 million Euros in the terminal year, to about 2.3% 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 2012 and 2013, and found the average rate is about 1% of revenue. Accordingly, it was assumed that in 2014, the investment will be 1% of total revenues, to maintain the existing, and during the forecast years the investment will increase to a rate of about 2.3% of total revenue. It was assumed that, in the terminal year, the investment will be equal to the depreciation.

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** - 46 days;
- **Other receivables days** – 3 days;
- **Inventory days -** 90 days;
- **Trade payables days -** 49 days;
- **Other payables days -** 28 days.

DCF Approach

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 30%, 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.

DCF Approach

Discount rate (WACC)

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%)

Where:

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 and Italy);
B=	Beta or systematic risk for this type of capital investment (in this case, the beta taken was for a period of five years, at a weekly section);
Rm–Rf=	Market risk premium; the expected return on a broad portfolio of stocks in the market (Rm) less the risk free rate (Rf);
SCP	Small cap premium - Ibbotson valuation edition 2013 yearbook;
Srp	Specific Premium.

DCF Approach

WACC

We based on the Capital Asset Pricing Model (**CAPM**) in calculating the WACC. The following table is the parameters that served for the calculation of the Unit's WACC, for December 31, 2013:

Parameter	Symbol	Value	Source
Unit's Debt	D/(D+E)	8.4%	Based on comparable companies analysis
Unit's Equity	E/(D+E)	91.6%	Based on comparable companies analysis
Cost Of Debt	Kd	1.95%	The Company's Cost of Debt
Tax Rate	T	30%	Effective tax rate of the unit
Beta	ß	0.75	Levered Beta - According to comparable companies
Risk Free Rate	Rf	1.61%	Index-linked governmental bond yields for 10-year (Bloomberg)
Market Premium	Rm-Rf	5.38%	Weighted Italy & Germany market risk premium (Damodaran)
SCP	SCP	6.03%	Ibbotson valuation edition 2012 yearbook
SRP	SRP	1.00%	Specific Premium
Cost Of Capital	Ke	12.65%	Rf +ß*(Rm-Rf)+SCP+SRP
Weighted average cost of capital	**WACC**	**11.71%**	D*(1-T)*Kd+E*Ke

Source: BDO analysis.

Rate of the ß section taken weekly over five years.

According to IAS 36, while measuring the recoverable amount, no income tax receipts or payments should be included. Therefore, we should measure a Pre-tax discount rate. According to our estimation the pre-tax discount rate totals to approximately 15.7%.

Terminal growth rate

The terminal growth rate of 2% was determined based upon the real economy expected growth rate in the long term.

DCF Approach

The Unit's Cash Flow

The following table shows the Unit's cash flow forecast, for December 31, 2012 and 2013 and for the forecast years 2014-2018 (thousands €):

€000	2012	2013	2014	2015	2016	2017	2018	Terminal
Revenue	**111,119**	**107,436**	**112,808**	**117,320**	**121,426**	**125,069**	**128,196**	**130,760**
Growth rate	*6.8%*	*-3.3%*	*5.0%*	*4.0%*	*3.5%*	*3.0%*	*2.5%*	*2.0%*
Total cost of sales	75,377	71,505	73,915	76,141	78,167	79,964	81,506	82,771
% of revenue	*67.8%*	*66.6%*	*65.5%*	*64.9%*	*64.4%*	*63.9%*	*63.6%*	*63.3%*
Gross profit	35,742	35,931	38,893	41,179	43,259	45,105	46,690	47,989
Gross margin	*32.2%*	*33.4%*	*34.5%*	*35.1%*	*35.6%*	*36.1%*	*36.4%*	*36.7%*
Operating expenses								
R&D	3,570	4,356	4,483	4,590	4,687	4,773	4,847	4,908
% of revenue	*3.2%*	*4.1%*	*4.0%*	*3.9%*	*3.9%*	*3.8%*	*3.8%*	*3.8%*
S&M	14,180	12,874	13,228	13,600	13,971	14,319	14,629	14,895
% of revenue	*12.8%*	*12.0%*	*11.7%*	*11.6%*	*11.5%*	*11.4%*	*11.4%*	*11.4%*
G&A	6,854	6,292	6,403	6,496	6,581	6,657	6,721	6,775
% of revenue	*6.2%*	*5.9%*	*5.7%*	*5.5%*	*5.4%*	*5.3%*	*5.2%*	*5.2%*
Total operating expenses	**24,604**	**23,522**	**24,114**	**24,686**	**25,239**	**25,748**	**26,198**	**26,577**
% of revenue	*22.1%*	*21.9%*	*21.4%*	*21.0%*	*20.8%*	*20.6%*	*20.4%*	*20.3%*
Pre tax operating profit	**11,138**	**12,409**	**14,779**	**16,493**	**18,020**	**19,357**	**20,492**	**21,412**
Pre tax operating margin	*10.0%*	*11.6%*	*13.1%*	*14.1%*	*14.8%*	*15.5%*	*16.0%*	*16.4%*
Adjustments								
Change in working capital	(317)	612	(879)	(777)	(756)	(689)	(524)	(388)
Depreciation	2,977	2,925	2,940	2,953	2,965	2,976	2,985	2,994
Capital expenditure	(900)	(1,600)	(1,470)	(1,772)	(2,075)	(2,380)	(2,687)	(2,994)
Net cash flow from operating activities	**12,898**	**14,347**	**15,370**	**16,897**	**18,153**	**19,263**	**20,267**	**21,024**
Number of periods			0.5	1.5	2.5	3.5	4.5	4.5
DCF			**14,288**	**13,576**	**12,605**	**11,560**	**10,510**	**79,533**

Source: BDO analysis and financial statements

Section 5

Recoverable Amount versus Carrying Amount Comparison

Recoverable Amount versus Carrying Amount Comparison

Carrying Amount

The following table presents the carrying amount calculation according to Management's information and unaudited consolidated financial statements for 31 December 2013, based on audited financial statements of the companies comprising the Unit (thousands €):

€000	2013
Accounts receivable	14,792
Other receivable	338
Inventory	16,663
Net Fixed Assets	17,270
Software	2,008
Total operational assets	**51,071**
Accounts payable	(9,583)
Other short-term liabilities	(5,821)
Pension Liability	(2,842)
Total operational liabilities	**(18,246)**
Customer relations and know How, net	15,983
Deferred tax (PPA)	(4,506)
Goodwill	75,579
Sub total	**87,056**
Total carrying amount	**119,881**

Source: Management information

If and only if, it is found that the recoverable amount of the asset is less than the book value, then the entity will be required to estimate impairment of the asset being measured and reduce it accordingly.

For finding the carrying amount of the activity, we examined the balance sheet of operations as of December 31, 2013.

Recoverable Amount versus Carrying Amount

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

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

€000	2013
Recoverable amount	142,072
Carrying amount	119,881
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.

Section 6
Appendix

Appendix

Sensitivity analysis

We examined the possible influence of changing the pre tax discount rate used in this report (**15.7%**) and the terminal growth rate (**2%**) on the value of the DCF-based Unit value.

The following table shows the predicted results following a change in the discount rate and terminal growth rates:

		Pre tax discount rate				
		13.7%	14.7%	15.7%	16.7%	17.7%
Terminal growth rate	1.0%	157,964	146,531	136,665	128,064	120,501
	1.5%	161,764	149,662	139,273	130,259	122,365
	2.0%	165,888	153,039	142,072	132,603	124,347
	2.5%	170,381	156,692	145,082	135,112	126,459
	3.0%	175,293	160,657	148,329	137,805	128,715

Source: BDO analysis

CHAPTER B

DIRECTORS' REPORT

B

FRUTAROM INDUSTRIES LTD.
DIRECTORS' REPORT OF THE COMPANY'S STATE OF AFFAIRS
FOR THE PERIOD ENDING DECEMBER 31, 2013

BOARD OF DIRECTORS' DISCUSSIONS OF 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 15,500 customers in more than 145 countries, and employing 2,700 people throughout the world.

Frutarom, one of the ten largest companies in the world in Flavors and Specialty Fine Ingredients, reports record results for 2013 in revenues, profit and earnings per share.

Frutarom's revenues grew from US$425 million and an EBITDA of US$66 million four years ago, to record revenues and profits of US$674 million and an EBITDA of US$116 million in 2013. Frutarom's revenues would have been US$784 million if the four acquisitions made by the company in 2013 had been consolidated from January 1, 2013.

Frutarom has two major activities, which are considered its core business: the Flavors activity and the Specialty Fine Ingredients activity the "**core business**").

- **The 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. Frutarom also develops new products to meet changing consumer preferences and future customer needs.

  In recent years, Frutarom's Flavors activity has grown in a rapid and profitable manner, through a combination of organic growth and acquisitions, and it currently constitutes 73% of Frutarom's total sales (compared to 33% in 2000). This accelerated growth is the result of the focus on the fast growing area of natural flavors, on development of innovation-based unique solutions combining taste and health for the large multi-national market segment, a focus on mid-size and local customers in emerging and developed markets (focusing in particular on private labels), 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 multi-national companies and as the result of Frutarom's strategic acquisitions, which have and are being successfully incorporated with Frutarom's global activities.

- **The 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, aroma chemicals, essential oils, unique citrus products, 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 portfolio of niche high value-added products, giving 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.

- **Trade and Marketing** – in addition to its core business, Frutarom also imports and markets various raw materials, not manufactured by Frutarom, as part of the service and comprehensive solutions it offers its customers. The trade and marketing activity is synergetic and supports Frutarom's core business as it leverages its global sales organization, supply chain and purchasing systems as well as global management, and allows Frutarom to offer a wider variety of products, solutions and more added value to its customers, mainly to medium sized and domestic ones, and to strengthen the partnership with its customers. This activity, which grew following the acquisitions of Etol and PTI, focuses mainly on Central and Eastern Europe and Israel. In 2013 sales from the Trade and Marketing activity came to US$39.7 million (5.9% of total Frutarom revenues).

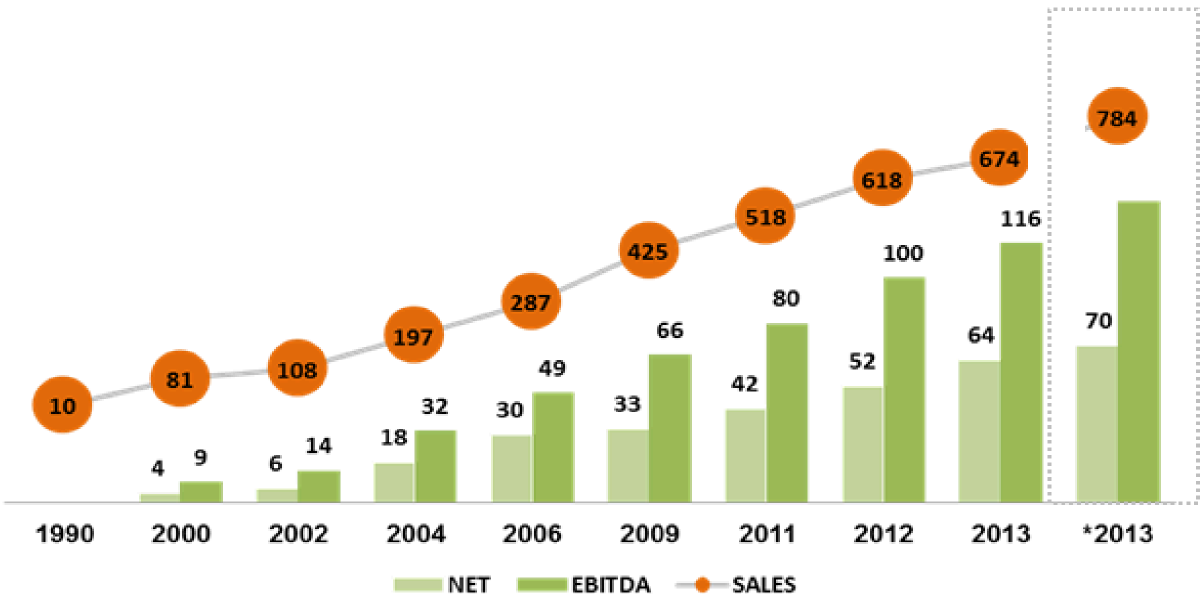
RAPID GROWTH STRATEGY – PROFITABLE ORGANIC GROWTH AND STRATEGIC ACQUISITIONS

Frutarom continues to act with determination to implement its rapid profitable growth strategy while strengthening its research and development, manufacturing, sales and marketing infrastructure and continuous search for additional strategic acquisitions.

Since 2000, Frutarom has grown at an average annual rate of 18%, through a combination of organic growth and the execution of 30 acquisitions. The Company's revenues over this period grew from US$81 million in 2000, to record of US$674 million in 2013, while its profit has grown from an EBITDA of US$9 million and net profit of US$4 million in 2000, to a record profit of US$116 million EBITDA and net profits of US$64 million in 2013. This year the Company generated US$89 million dollar of operating cash flow.

Frutarom revenues would have been approx. US$784 million, if the revenues from the four acquisitions made this year had been consolidated on January 1, 2013.

Development of Frutarom sales



- 2013 – Frutarom sales and net profit combined with the four acquisitions made in 2013, had they been acquired and consolidated on Jan. 1, 2013.

- **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 of the Flavors activity currently constitute 73% of total Frutarom's revenues compared to 33% in 2000. The Company estimates that the rapid growth trend will continue even under today's challenging market conditions.

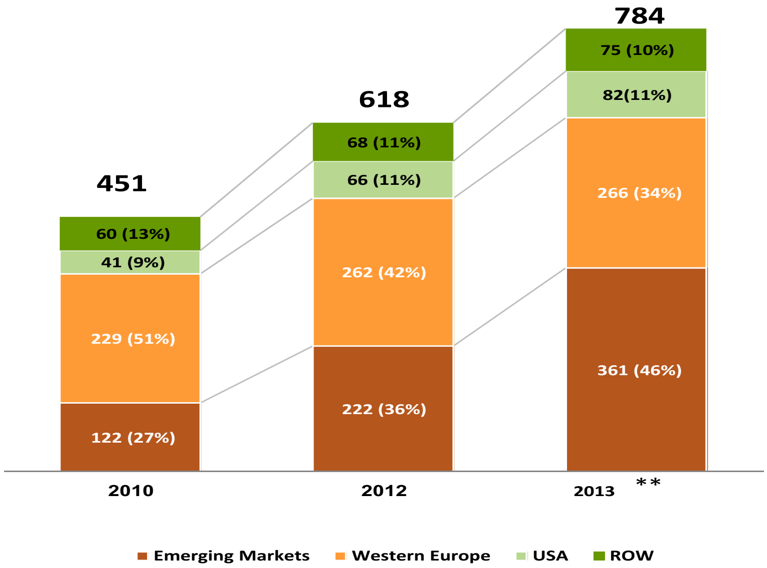
- **<u>Development of New Products and Solutions Combining Taste and Health</u>** - Frutarom develops innovative flavor and health solutions addressing customers' requirements and future needs. These solutions are in line with the major trends in the global food market and with consumer demand, including 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 and health give the Company an important competitive advantage among customers in both developed and emerging markets. These new and innovative products are for the main part of higher margins, and therefore contribute not only to a growth in sales but also to Frutarom's improved product mix and profitability.

- **<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 of its margins. Frutarom anticipates continued improved results for the Specialty Fine Ingredients activity also as a result of the successful introduction of new and innovative products that are currently in the pipeline.

- **<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, resulted in Frutarom's revenues this year (combined with the acquisitions made this year, had they been consolidated from the beginning of the year) tripling in developing markets, and doubling in the United States (compared to 2010). At the same time, the Flavors activity in the United States grew by a factor of four. As a result of this massive growth the revenues of Frutarom in Western Europe were reduced from 51% in 2010 to 34% this year.

  The five acquisitions made by Frutarom in 2013 and in the beginning of 2014 (JannDeRee in South Africa, PTI in Russia – with sales in additional locations in Eastern Europe, Aroma in Guatemala, Hagelin in the United States -with significant sales in Africa and in Latin America - and the American CitraSource) will all contribute to Frutarom's accelerated growth and to an increase in market share in emerging markets and in the United States in the coming years.

Frutarom Revenues – By Geographic Regions 2010-2013:



- Frutarom sales after the four acquisitions made in 2013, had they been acquired and consolidated on Jan. 1, 2013.

Frutarom focuses and will continue to invest a great deal of resources on accelerating growth and increasing the share of its revenues from emerging markets and the United States among other things by focused strengthening of its R&D, production, marketing and sales infrastructures in important target countries and execution of additional strategic acquisitions.

At the same time Frutarom continues to expand its activities in the markets of Western Europe, and will continue doing so. The major countries in Western Europe report signs that mark an end to the recession and a slow return to growth, and if this trend continues it will contribute to the improvement of the growth in sales in these important markets.

- **Focus on providing quality service and product development for large multi-national customers and for medium size 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. Frutarom will continue to focus on providing niche value added products to the large multinational food and beverage manufacturers and on expanding its portfolio of natural food solutions. For the 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 dates of delivery.

- **Acquisitions and Mergers, and their contribution to the achievement of 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 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, and in the beginning of 2014 made a further acquisition of the American CitraSource.

  - **Acquisition of JannDeRee -** On May 2, 2013 Frutarom acquired 100% of the share capital of the South African flavors company JannDeRee for USD 5.0 million. The company was consolidated into Frutarom’s statements on May 1, 2013.

    JannDeRee, founded in 1993, develops, manufactures, and markets flavors with an emphasis on savory flavors and sweet flavor solutions. JannDeRee, which over the past few years has grown at a fast pace, has a development, production and marketing site in Johannesburg, South Africa, to which Frutarom activities in South Africa were transferred following the acquisition. JannDeRee also has a wide customer base in South Africa and in other important emerging countries in the sub-Sahara region such as Malawi, Zimbabwe and Mozambique. JannDeRee’s activities are synergetic with Frutarom’s activities in South Africa in the field of flavors, which have grown at rates higher than the rate of market growth over the past few years.

    The Integration of JannDeRee into Frutarom's activity in South Africa was completed over the third quarter of 2013, including integration of sites, management, purchasing, production and supply chain systems, and integration of the research and development, marketing and sales systems.

    For further information regarding the acquisition of JannDeRee, see the Company’s immediate report published on May 2, 2013.

- **Acquisition of PTI** - on November 20, 2013 Frutarom completed 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") for US$50.3 million.

  PTI, established in 1996, develops, manufactures and markets 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. PTI has two production sites near Moscow and a state of the art R&D, marketing and sales center including development and application labs, and approximately 15 distribution centers throughout Russia and other countries in the region.

  In the year ending December 31, 2013, PTI's sales turnover stood at 115.2 million. PTI's savory flavor solution sales, its central core activity, grew at a rate higher than the market growth rate over the past few years, reaching US$66 million in 2013. PTI's flavors' activity has similar profitability rates to Frutarom's, into which it has been integrated. PTI also has trade and marketing activity which it provides as part of the comprehensive solution it offers to its customers, including raw materials not manufactured by PTI. The scope of this activity, which has been integrated into Frutarom's trade and marketing activities (not one of Frutarom's core activities) reached US$49 million in 2013, and has similar profitability rates to Frutarom's trade and marketing activity. PTI was consolidated into Frutarom's reports on October 1, 2013.

  Frutarom's is acting to leverage of PTI's R&D, marketing and sales infrastructure in Russia and in the markets in Central and Eastern Europe in which it operates, as well as Frutarom's global distribution and sales infrastructure, in order to leverage and realize the many cross-selling opportunities this acquisition brings, by expanding the customer base and of Frutarom's product portfolio. The integration of PTI's activities with Frutarom's in the countries in which the two companies operate will present additional synergies as well as achieving significant operational savings.

  For further information regarding the acquisition of PTI, see the Company's immediate reports published on November 18 and 20, 2013.

- **Acquisition of Aroma S.A.** – on November 25, 2013 Frutarom acquired the International Aroma Group, a Panama company, holder of the Guatemalan Aroma group ("Aroma"), in return for a cash payment of US$13 million. The share purchase agreement contains a mechanism for payment of future consideration, under which an additional payment will be made at the rate of the EBITDA achieved above US$2.25 million over the years 2013 to 2015, and a price adjustment mechanism based on net assets as at November 30, 2013.

Aroma, established in 1990, develops, manufactures and markets flavor solutions, including mainly sweet flavors for beverages, dairy products, confectionary, snack food and convenience foods. Aroma has 57 employees, 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 Central America.

Aroma's sales turnover in the year ending December 31, 2013 stood at US$6.2 million.

The acquisition of the Guatemalan Aroma joins the acquisition of the Brazilian Mylner completed by Frutarom at the beginning of 2012, and to Frutarom's independent operations in Costa Rica, which includes a development lab and sales and marketing infrastructure that is now integrated with Aroma activities. The acquisition will allow Frutarom to strengthen its position and presence in these important markets of Central and South America, while expanding its product portfolio and increasing its research and development, 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.

- **Acquisition of Hagelin** – on December 12, 2013 Frutarom acquired 100% of the share capital of the US based Hagelin and the US based BRC Operating Company LLC (jointly: "**Hagelin**"), in return for a cash payment of US$52.4 million. Hagelin's sales turnover reached US$23.6 million in 2013. The company was consolidated into Frutarom's balance sheet on December 31, 2013.

  Hagelin, founded in 1967, produces and markets flavors and unique flavor technologies for the food industry, with an emphasis on the growing area of beverage flavors. Hagelin has higher profitability rates than the profitability rates of Frutarom's Flavors sector (the most profitable of Frutarom's sectors) into which it will be integrated.

  Hagelin's sales turnover in the year ending December 31, 2013 stood at US$23.6 million.

  Hagelin's activity in the UK has already been integrated into Frutarom's activities in the UK, and Frutarom is working towards integrating Hagelin's activities in the US and utilizing the many synergies in all areas which this acquisition brings.

  For further information regarding the acquisition of Hagelin, see the Company's immediate report published on December 12, 2013.

- **Acquisition of CitraSource** - on February 25, 2014, Frutarom acquired the business and assets of the US based CitraSource for a consideration of US$7.5 million, plus an additional future payment based on CitraSource's profit before tax in the years 2014-2018.

  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 its area of operations, which will contribute to Frutarom's global purchase system. CitraSource's activities will be integrated into the Specialty Fine Ingredients division starting from the date of purchase, in the first quarter of 2014.

  For further information regarding the acquisition of CitraSource, see the Company's immediate report published on February 25, 2014.

Increase in Profit and Profit Margins

- **Contribution and integration of acquisitions -** Integration of the eight acquisitions made in 2011 and 2012 was performed successfully and according to plan, and these acquisitions have already contributed not only to Frutarom's growth in sales but also to the significant improvement in profits this year. Frutarom continues to realize the many cross-selling opportunities and enhanced technological capacities resulting from these acquisitions, and to realize the savings resulting from the integration of R&D, sales, marketing, supply chain, operations and purchasing infrastructures. The full potential of the synergies presented by the acquisitions has not yet been realized, and Frutarom is working to maximize the many benefits from these integrations. Integration of the five acquisitions made in 2013 and in the beginning of 2104 is moving ahead successfully, and these are expected to contribute to Frutarom's continued growth in sales and profit starting already in 2014 and in the coming years.

- **Integration of R&D systems -** Frutarom is working to maximally utilize the many research, development, innovation and technological capacities is has gained over the last few years following the acquisitions, and to implement a new system for managing customers and R&D projects and applications, both on a site level and by connecting between its various R&D sites specializing in the same selection of products. The system will contribute to more focused and efficient management of the R&D efforts across the group and of the development and implementation of the unique solutions for customers, while achieving optimal cross-company solutions and increasing customer satisfaction.

- **Strengthening Global Purchasing -** Frutarom continues to build and strengthen its global purchasing infrastructure, leveraging its size following the recent acquisitions, while 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 capitalizing on the harmonization of the raw materials used in the development and manufacture of all of its products.

- **Operational Efficiencies - Operational Savings** - Frutarom is continually planning, executing and implementing more projects for the unification between and consolidation of production sites, and is striving to achieve efficiency in logistics and supply chain which will contribute to strengthening its competitive advantage and improving its profit margins over the coming years.

Frutarom expects that the continued execution of its rapid and profitable growth strategy, the continued stabilization of prices of the raw materials it uses in the manufacture of its products and the strengthening of its global purchasing system, together with the contribution of the operational efficiency efforts, improvement of its costs structure, optimal utilization of its productions sites throughout the world and the successfully integration of recent acquisitions, will result in a continuing trend of improved profit and margins.

Frutarom's capital structure (total assets of US$970.8 million and equity of US$521.1 million as of December 31, 2013, constituting 53.7% of the total assets) and net debt (total loans after deduction of cash), which stands at US$190.7 million as of December 31, 2013, supported by the strong cash flow it achieves from operating activities, together with bank backing, will allow Frutarom 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 STATUS

The Group's total assets as of December 31, 2013 were US$970.8 million compared with US$772.4 million as of December 31, 2012.

The Group's current assets as at December 31, 2013 totaled US$375.0 million, compared with US$301.0 million as of December 31, 2012.

The fixed assets after deduction of cumulative depreciation and other assets net as of December 31, 2013 totaled US$592.3 million, compared with US$468.0 million as of December 31, 2012.

The rise in the total assets is mainly due to acquisitions made in 2013.

C. RESULTS OF OPERATIONS IN 2013

2013 was another record year for Frutarom. Sales grew by 9% reaching US$674 million, and record highs were also achieved in gross profit, operating profit, EBITDA, net profit 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, continues. Gross margin from core business (net of one-time expenses) increased, reaching 39.8% in 2013 compared with 37.6% in 2102, and operating margin in 2013 from core business (net of one-time expenses) reached 14.3%, compared with 12.3% last year.

Net profit and earnings per share (net of one-time expenses) increased by 28.3% and 27.0%, respectively, in 2013, reaching US$67.5 million and US$1.16, compared with US$52.6 million and 0.91 in 2012.

The integration and operational efficiency projects and processes, which as stated include consolidation of production sites and activities and transfer of activities to countries where operational costs are lower, have begun to contribute to an improvement in the Company's results in the second half of 2013. These projects, together with additional activities planned for 2014 and continued building of global purchasing system, will contribute to the continued improvement of the Company's results over the next years.

Sales

In 2013, Frutarom sales, grew by 9% reaching a yearly record high of US$673.7 million, compared with US$618.0 million in 2012. Currency effect was negligible. The acquisitions made over 2013 contributed US$37 million to sales over the period. Net of the contribution of the acquisitions, sales grew by 3% this year.

Flavor sales increased by 8.1% compared with last year, reaching a record high of US$494.4 million, compared with US$457.3 million in 2012, constituting 73% of total Frutarom sales. Accelerated growth in Flavors, the most profitable among Frutarom's activities, is the result of organic growth and of the acquisitions, which contributed US$21.7 million. Net of the contribution of these acquisitions, Flavor sales grew by 3.3% this year.

Frutarom's sales in Specialty Fine Ingredients increased by 3.4%, reaching US$145.6 million, compared with US$140.8 million in 2012. The innovative high added value products developed in the Company's labs over the last few years contributed to the profitable growth in the Specialty Fine Ingredients activity.

Frutarom's sales in Trade and Marketing (which is not a core business) increased by US$17.4 million compared with 2012, reaching US$39.7 million. This activity, which increased following the acquisition of Etol and PTI, focuses mainly on Central and

Eastern Europe and Israel. PTI's trade and marketing activity acquired in the fourth quarter of the year, contributed most of the growth in sales - US$15.3 million.

Sales Breakdown by Fields of Activity 2002-2013 (US$ M and %)

		2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Flavor Activity	Sales	45.3	68.2	110.9	150.4	187.0	247.7	339.8	297.1	306.4	369.9	457.3	494.4
	%	42%	49%	56%	62%	65%	67%	72%	70%	68%	71%	74%	73%
Fine Ingredient Activity	Sales	57.7	67.0	81.7	89.8	98.4	115.0	124.3	123.8	141.5	145.0	140.8	145.6
	%	54%	48%	41%	37%	34%	31%	26%	29%	31%	28%	23%	22%
Inter activities	Sales	-1.7	-2.3	-2.6	-2.7	-4.9	-4.9	-4.0	-2.8	-2.2	-2.9	-2.4	-6.0
Total core business	Sales	**101.3**	**132.8**	**190.0**	**237.5**	**280.5**	**357.8**	**460.1**	**418.1**	**445.7**	**512.0**	**595.7**	**634.0**
	%	**94%**	**95%**	**96%**	**97%**	**98%**	**97%**	**97%**	**98%**	**99%**	**99%**	**96%**	**94%**
Trade & Marketing	Sales	6.2	6.5	6.8	6.3	6.7	10.5	13.2	7.1	5.4	6.4	22.3	39.7
	%	6%	5%	4%	3%	2%	3%	3%	2%	1%	1%	4%	6%
Total Sales		107.5	139.3	196.8	243.8	287.2	368.3	473.3	425.2	451.1	518.4	618.0	673.7

The following is a summary of the profit and loss report for 2011 - 2013 (US$ M):

In 2013 Frutarom achieved record highs in sales, gross profits, operating profit, EBITDA, net profit, and earnings per share.

	2011	2012	2013	Change (%) 2011-2013
Sales of the Group	518.4	618.0	673.7	9.0%
Sales of core business (Flavors and Specialty Fine Ingredients)	512.0	595.7	634.0	6.4%
Gross profit from core business (net of one-time expenses)	**187.5**	**223.6.0**	**252.5**	**12.7%**
Gross profit of the Group (net of one-time expenses)	188.6	226.7	258.5	14.1%
Gross profit of the Group	188.6	226.3	256.8	13.5%
R&D, Sales, G&A and Other expenses (net of one-time expenses)	128.0	152.3	166.7	9.4%
R&D, Sales, G&A and Other expenses	129.9	153.4	170.0	10.8%
Operating profit from core business (net of one-time expenses)	60.3	73.3	91.0	24.1%
Operating profit of the Group (net of one-time expenses)	60.6	74.3	91.9	23.6%
Operating profit of the Group	58.7	72.8	86.8	19.1%
EBITDA from core business (net of one-time expenses)	**82.0**	**100.9**	**119.5**	**18.4%**
EBITDA of the Group (net of one-time expenses)	82.3	101.9	120.5	18.2%
EBITDA of the Group	80.4	100.4	116.0	15.5%
Financing Expenses	5.8	7.2	7.5	4.0%
Profit before tax	52.9	65.6	79.2	20.8%
Net profit of the Group (net of one-time expenses)	**42.4**	**52.6**	**67.5**	**28.3%**
Net profit of the Group	42.0	52.0	63.6	22.4%

Gross Profit

Gross profit of Frutarom's core business (which include the Flavors and Specialty Fine Ingredients activities) net of one-time expenses for acquisitions in the amount of US$1.8 million, increased by 12.7% reaching US$252.5 million. Gross margin of core business (net of said one-time expenses) reached 39.8% compared with gross margin of 37.6% in 2012.

Gross profit of all Frutarom activities (net of one-time expenses) increased by 14.1% to US$258.5 million (38.4% of all revenues) compared with US$226.7 million (36.7% of all revenues) in 2012.

Gross profit of all Frutarom activities (including one-time expenses) increased by 13.5% reaching an annual record high of US$256.8 million (38.1% of all revenues) compared with US$226.3 million (36.6% of all revenues) in 2012.

Organic growth in sales, improved product mix in the core business and stability in the prices of raw materials Frutarom uses in the manufacture of its products all contributed to the improvement in gross profit and margin. The effect of the actions taken by Frutarom in order to utilize the many operational synergies resulting, among other things, from recent acquisitions, has only partially been realized in 2013 and will continue to come to fruition and contribute to the results in 2014 and beyond. Frutarom continues to build and strengthen its global purchasing system, utilizing its increased purchasing power from the recent 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

In 2013, R&D, sales and marketing, G&A and other expenses totaled US$170 million (25.2% of sales, and 24.7% net of one-time expenses), compared with US$153.4 million (24.8% of sales and 24.6% net of one-time expenses), compared with last year.

R&D, Sales and marketing expenses, G&A and other expenses included one-time expenses of US$3.4 million, most as the result of the closing of one of Frutarom's sites in north Germany and transfer of its activities to other more efficient sites of the Company, as part of the previously stated operational efficiencies plan and one-time expenses resulting from acquisitions made this year.

Over the same period last year, sales and marketing, R&D, G&A and other expenses included onetime expenses for acquisitions, which came to US$1.1 million.

The increase in expenses is the result of the increase in the scope of activities, and mainly from the acquisitions made in 2012 and 2013. As previously stated, Frutarom continuously acts to achieve maximum efficiency, improve its cost structure, develop a global purchasing system and strengthen its future competitive capabilities, while maximally utilizing its sites throughout the world and successfully integrating its most recent acquisitions.

Operating Profit and EBITDA

In 2013, operating profit in Frutarom's core business (which include the Flavors and Specialty Fine Ingredients activities), net of one-time expenses, increased by 24.1%, reaching US$91.0 million (14.3% of sales), compared with US$73.3 million (12.3% of sales) in 2012.

Operating profit of all Frutarom activities (net of said one-time expenses) increased in 2013 by 23.6% to US$91.9 million (13.6% of all sales).

Operating profit of all Frutarom activities (including the one-time expenses) increased in 2013 by 19.1%, reaching a yearly record high of US$86.8 million (12.9% of sales), compared with US$72.8 million (11.8% of sales) last year.

EBITDA in 2013 from Frutarom's core business (which include the Flavors and Specialty Fine Ingredients activities), net of one-time expenses, increased by 18.4%, reaching US$119.5 million (18.8% of sales), compared with US$100.9 million (16.9% of sales) in 2012..

The EBITDA of all Frutarom activities (net of one-time expenses) for 2013 increased by 18.2%, reaching a yearly record high of US$120.5 million (17.9% of sales) compared with US$101.9 million during the same period last year (16.5% of sales).

The EBITDA of all Frutarom activities (including one-time expenses) for 2013 increased by 15.5%, reaching a yearly record high of US$116.0 million (17.2% of sales) compared with US$100.4 million during the same period last year (16.2% of sales).

Financing Expenses / Income

In 2013, financing expenses totaled US$7.5 million (1.1% of sales), compared with US$7.2 million in 2012 (1.2% of sales).

Interest expenses in 2013 totaled US$5.6 million, compared with US$7.2 million over the same period last year. The reduction in interest expenses derived from a decrease in interest rates and a decrease in the Company's average debt level for the year.

In 2013 financing expenses from exchange differentials came to US$1.9 million, compared with negligible exchange differentials in 2012. The increase in financing expenses relating to exchange differentials derived from the weakening of the exchange rate of the dollar versus Western European currencies and its strengthening versus Eastern European currencies.

Profit before Tax

In 2013, profit before tax went up by 20.8%, reaching a yearly record high of US$79.2 million (11.8% of sales), compared with US$65.6 million (10.6% of sales) in 2012.

Taxes on Income

In 2013, taxes on income totaled US$15.6 million (19.7% of profit before tax) compared with US$13.6 million (20.8% of profit before tax) in 2012.

Net Profit

Net profit of all Frutarom activities for 2013, net of one-time expenses increased by 23.8%, reaching a yearly record high of US$67.5 million, compared with US$52.6 million in 2012. Net margin reached 10.0% in 2013, compared with 8.5% in 2012.

In 2013, net profit including one-time expenses increased by 22.4%, reaching a yearly record high of US$63.6 million, compared with US$52.0 million in 2012. Net margin reached 9.4% in 2013, compared with 8.4% in 2012.

Earnings per Share

Earnings per share in 2013 (net of one-time expenses) increased by 27.0% reaching a record high of US$1.16 compared with US$0.91 last year.

Earnings per share (including one-time expenses), increased by 21.1% reaching a record high of US$1.09 compared with US$0.9 per share last year.

RESULTS OF OPERATIONS IN Q4 2013

Q4 2013 was again a record quarter, in which Frutarom achieved record highs in sales, reaching US$191.8 million, in gross profit, operating profit, EBITDA, net profit and earnings per share.

This trend of improvement in gross and operating profit and margin is continuing. Gross margin from Frutarom's core business (which include the Flavors and Specialty Fine Ingredients activities) net of one-time expenses has increased, reaching 39.5% in Q4 2013, compared with 36.5% in Q4 2012. Operating margin from Frutarom's core business (net of one-time expenses) in this quarter reached 13.3%, compared to 10.6% in the same quarter last year. EBITDA from Frutarom's core business (net of one-time expenses) reached US$30.7 million (17.9% of sales).

Net profit and earnings per share (net of one-time expenses) increased over Q4 2013 by 49.9% and 49.2% respectively, reaching US$17.2 million and US$0.29, respectively, compared with US$11.5 million and US$0.20 in the same quarter last year.

Integration and operational efficiency projects, which include, as mentioned, consolidation of production sites and activities and transfer of activities to countries where operating costs are lower, contributed to the improvement in Frutarom results in Q4 2013. These projects and processes, together with additional operational efficiency activities planned for 2014 and the continued building of a global purchasing system, will contribute to the continuing improvement in Frutarom results in the years to come.

Sales

In Q4 2013, Frutarom sales grew by 32.4%, reaching a fourth quarter record high of US$191.8 million, compared with US$144.9 million during Q4 2012. Currency effects contributed to growth in sales this quarter by 1.6% (US$2.3 million). The acquisitions made in the quarter contributed US$35.9 million to sales over the quarter. Net of the contribution of the acquisitions and currency effects, organic growth this quarter reached 6.2% compared with Q4 of last year.

Flavors sales in Q4 2013 increased by 24.6%, reaching a fourth quarter record high of US$139.3 million, compared with US$111.7 during the same quarter last year, constituting 73% of total Frutarom sales. Currency effect contributed 1.6% to growth. The acquisitions made in 2013 contributed US$20.6 million to sales in Flavors during this quarter. Organic growth in Flavors net of the contribution of the acquisitions and currency effect reached 4.6% this quarter in comparison with Q4 of 2012.

Specialty Fine Ingredients sales increased in Q4 2013 by 14.4%, reaching US$33.8 million compared with US$29.5 million in the same quarter last year. Currency effect this quarter contributed 1.5%. Organic growth in Specialty Fine Ingredients was 12.9% compared with the same quarter last year. New innovative high added value products developed in the Company's labs over the last few years contributed to organic growth in Specialty Fine Ingredients.

Frutarom sales in Trade and Marketing (not one of Frutarom's core activities) increased by US$15.6 million in Q4 2013, achieving US$19.9 million compared with US$4.3 million in the same quarter last year. This activity, which grew as a result of the acquisition of ETOL and PTI, focuses mainly on Central and Eastern Europe and Israel. The trade and marketing activity of PTI, acquired this quarter, contributed most of the increase in sales this quarter - US$15.3 million.

Sales Breakdown by Activity for Q4 2002-2013 (US$ M and %)

		Q4 2002	Q4 2003	Q4 2004	Q4 2005	Q4 2006	Q4 2007	Q4 2008	Q4 2009	Q4 2010	Q4 2011	Q4 2012	Q4 2013
Flavors Activity sales	**Sales**	10.4	18.5	40.1	30.8	45.5	78.5	71.3	76.6	78.1	100.1	111.7	139.3
	%	44%	51%	70%	59%	63%	72%	72%	71%	69%	76%	77%	73%
Fine Ingredient Activity sales	**Sales**	12.1	17.2	16.1	20.0	26.4	28.9	25.5	30.9	33.2	30.9	29.5	33.8
	%	51%	47%	28%	38%	36%	27%	26%	29%	30%	23%	20%	18%
Inter activities	**Sales**	-0.5	-0.6	-0.7	0.5	-1.4	-1.5	-0.8	-0.4	-0.5	-0.5	-0.7	1.1
Core business Sales	**Sales**	22.0	35.1	55.5	51.3	70.5	105.9	96.0	107.1	110.8	130.5	140.6	174.2
	(%)	94%	96%	97%	98%	97%	98%	97%	99%	99%	99%	97%	90%
Trade & Marketing	**Sales**	1.5	1.4	1.5	1.3	2.0	2.6	2.7	1.4	1.6	1.1	4.3	19.9
	%	6%	4%	3%	2%	3%	2%	3%	1%	1%	1%	3%	10%
Total sales		23.5	36.5	57.0	52.6	72.5	108.5	98.7	108.5	112.4	131.6	144.9	191.8

<u>The following is a summary of the profit and loss report for Q4 in the years 2011-2013:</u>

In Q4 2013 Frutarom again achieved record fourth quarter highs in sales, gross profits, operating profit, EBITDA, net profit and earnings per share.

	Q4 2011	**Q4 2012**	**Q4 2013**	**Change (%) 2011-2013**
Sales of the Group	131.6	144.9	191.8	32.4%
Sales of core business – Flavors and Specialty Fine Ingredients	130.5	140.6	171.9	22.3%
Gross profit from core business (net of one-time expenses)	**46.5**	**51.4**	**67.9**	**32.1%**
Gross profit of the Group (net of one-time expenses)	46.8	51.9	71.9	38.6
Gross profit of the Group	46.8	51.5	70.2	36.3%
R&D, Sales, G&A and Other expenses (net of one-time expenses)	34.2	36.9	48.7	32.0%
R&D, Sales, G&A and Other expenses	34.6	37.8	49.9	32.0%
Operating profit from core business (net of one-time expenses)	**12.5**	**14.8**	**22.9**	**54.1%**
Operating profit of the Group (net of onetime expenses)	12.6	15.0	23.3	55.1%
Operating profit of the Group	12.2	13.7	20.3	48.4%
EBITDA from core business (net of one-time expenses)	**18.4**	**21.8**	**30.7**	**41.0%**
EBITDA of the Group (net of onetime expenses)	18.5	21.9	31.2	42.1%
EBITDA of the Group	18.1	20.7	28.3	36.9%
Financing Expenses	3.2	1.4	2.5	78.8%
Profit before tax	8.9	12.3	17.8	44.9%
Net profit of the Group (net of one-time expenses)	**8.1**	**11.5**	**17.2**	**49.9%**
Net profit of the Group	7.9	10.5	15.0	41.9%

Gross Profit

Gross profit in Frutarom's core business (Flavors and Specialty Fine Ingredients activities), net of one-time expenses, mainly for acquisitions, in the amount of US$1.7 million, increased in Q4 2013 by 32.1% reaching US$67.9 million. Gross profit from core business (net of said one-time expenses) in Q4 2013 reached 39.5%, compared with 36.5% in Q4 2012.

Gross profit in Q4 2013 for all Frutarom activities (net of one-time expenses) increased by 38.6% reaching a record fourth quarter high of US$71.9 million (37.5% of revenues), compared with US$51.9 million (35.8% of revenues) in the same quarter in 2012.

The gross profit of all Frutarom activities (including one-time expenses) increased in Q4 2013 by 36.3%, reaching a fourth quarter high of US$70.2 million (36.6% of revenues) compared with US$51.5 million (35.5% of revenues) in Q4 2012.

Organic growth in sales, the improvement in the product mix of Frutarom's core business and stability in the prices of the raw materials Frutarom uses in the manufacture of its products contributed to the improved gross profit and margin. The effect of the actions taken by Frutarom in order to utilize the many operational synergies resulting, among others, from recent acquisitions, has only partially been realized in 2013 and will continue to come to fruition and contribute to its results in 2014 and beyond. Frutarom continues to build and strengthen its global purchasing system, utilizing its added purchasing power from its recent acquisitions and continuously expanding its pool of suppliers with an emphasis on purchase of the 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 continuation of 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 came to US$49.9 million (26.0% of sales and 24% net of one-time expenses) in Q4 2013 compared with US$37.8 million in Q4 2012 (26.1% of sales and 25.4% net of one-time expenses).

R&D, Sales and marketing expenses, G&A and other expenses in Q4 2013 included one-time reorganization and acquisition expenses in the amount of US$1.2 million. During the same period last year, sales and marketing, R&D, G&A and Other expenses included one-time expenses for acquisitions in the amount of US$0.9 million.

The increase in expenses derives from the increase in the scope of activities, mainly from the acquisitions made in 2012 and 2013. Frutarom has and continues to act as stated to achieve maximal efficiency, for the improvement of its cost structure, developing a global purchasing system and strengthening of its future competitive capabilities, while taking maximum advantage of its sites throughout the world and successfully integrating its latest acquisitions.

<u>Operating Profit and EBITDA</u>

In Q4 2013, operating profit from Frutarom's core business (Flavors and Specialty Fine Ingredients), net of one-time expenses (in the amount of US$2.9 million) increased by 54.1% reaching US$22.9 million (13.3% of sales) compared with US$14.8 million (10.6% of sales) in the same quarter last year.

Operating profit of all Frutarom activities in Q4 2013 (net of one-time expenses) increased by 55.1%, reaching a fourth quarter high of US$23.3 million (12.1% of sales) compared with US$15.0 million (10.4% of sales) in the same quarter last year.

Operating profit of all Frutarom activities in Q4 2013 (including one-time expenses) increased by 48.4% reaching a fourth quarter high of US$20.3 million (10.6% of sales) compared with US$13.7 million (9.5% of sales) for the same quarter last year.

EBITDA for Frutarom's core business in Q4 2013 net of one-time expenses increased by 41.0%, reaching US$30.7 million (17.9% of sales) compared with US$21.8 million during the same period last year (15.5% of sales)

EBITDA of all Frutarom activities in Q4 2013 (net one-time expenses) increased by 42.1% reaching a fourth quarter high of US$31.2 million (16.2% of sales) compared with US$21.9 million (15.1% of sales) for the same period last year.

The EBITDA of all Frutarom activities in Q4 2013 (including one-time expenses) increased in Q4 by 36.9% reaching a fourth quarter high of US$28.3 million (14.7% of sales) compared with US$20.7 million (14.3% of sales) for the same period last year.

<u>Financing Expenses / Income</u>

In Q4 2013, financing expenses came to US$2.5 million (1.3% of sales) compared with financing expenses of US$1.4 million (1.0% of sales) in the same quarter last year.

Following the increase in Frutarom's loans taken for the purpose of financing acquisitions over this quarter, interest expenses in Q4 2013 increased to US$2.0 million, compared with US$1.6 million in the same period last year.

The increase in financing expenses for exchange differentials reached US$0.5 million, compared with financing income of US$0.2 in the same quarter last year.

The increase in financing expenses for exchange differentials derives from the strengthening of the exchange rate of the dollar versus other currencies (mainly the Turkish lira, the South African rand, Eastern European currency and the NIS) as of December 31, 2013, compared with the exchange rate of the dollar versus the same currencies as of September 30, 2013.

Profit before Tax

In Q4 2013, profit before tax increased by 44.9%, reaching a fourth quarter record high of US$17.8 million (9.3% of sales), compared with US$12.3 million (8.5% of sales) in Q4 2012.

Taxes on Income

Taxes on income in Q4 2013 came to US$2.9 million (16.1% of profit before tax) compared to US$1.8 million during the same quarter last year (14.3% of profit before tax).

Net Profit

In Q4 2013, net profit (net of one-time expenses) increased by 49.9% reaching US$17.2 million, 9% of sales, compared with US$11.5 million in fourth quarter last year (7.9% of sales).

Net profit in Q4 2013 (including one-time expenses) increased by 41.9%, reaching a fourth quarter high of US$15.0 million, compared with US$10.5 million in Q4 2012. Net margin totaled 7.8%, compared with 7.3% in Q4 2012.

Earnings per Share

Earnings per share in Q4 2013 (net of one-time expenses) increased by 49.2%, achieving a record high of US$0.29 per share, compared with US$0.2 per share in Q4 2012.

Earnings per share in Q4 2013 (including one-time expenses) increased by 41.3%, achieving a fourth quarter record high of US$0.26 per share, compared with US$0.18 per share in Q4 2012.

Summary of the quarterly profit and loss reports for 2011 - 2013 (US$ M):

	Q1 2011	Q2 2011	Q3 2011	Q4 2011	Q1 2012	Q2 2012	Q3 2012	Q4 2012	Q1 2013	Q2 2013	Q3 2013	Q4 2013
Income	121.0	130.6	135.3	131.6	151.2	164.8	157.1	144.9	152.2	168.6	161.0	191.8
Gross profit	45.7	48.5	47.7	46.8	54.9	61.8	58.1	51.5	57.2	66.9	62.6	70.2
Selling, Marketing, R&D, G&A and Other Expenses	29.0	31.5	34.8	34.6	37.1	40.0	38.5	37.8	38.3	41.9	40.0	49.9
Operating profit (net of one-time expenses)	16.7	17.2	14.2	12.6	17.6	22.2	19.5	15	19.0	27.0	22.6	23.3
Operating profit	16.6	17.0	12.9	12.2	17.8	21.8	19.5	13.7	18.9	24.9	22.6	20.3
EBITDA (net of one-time expenses)	21.6	22.4	19.9	18.5	24.7	28.9	26.3	21.9	25.9	33.9	29.5	31.2
EBITDA	21.5	22.2	18.6	18.1	25.0	28.5	26.3	20.7	25.8	32.6	29.4	28.3
Finance expenses	-0.9	0.8	2.6	3.2	0.9	4.3	20.6	1.4	1.4	2.3	1.3	2.5
Profit before tax	17.5	16.2	10.3	8.9	16.9	17.5	18.9	12.3	17.5	22.6	21.3	17.8
Net profit	13.1	12.3	8.7	7.9	13.5	13.5	14.4	10.5	14.0	17.6	17.0	15.0

Seasonality

The Company's business is affected by seasonal fluctuations, which until recently were reflected in higher sales and profitability in the first half of any given year, and lower sales and profitability during the second half of any given year (particularly in the fourth quarter of each year). A substantial portion of the Company's products is used by its customers in the manufacture of beverages and milk products such as soft drinks, ice cream and yogurt, for which demand increases during the summer months. As a result, the Company's sales of certain flavors and raw materials increase over the first half of the year, as beverage and milk product manufacturers increase supply and production in advance, in anticipation of increased demand in the summer months. The impact of these fluctuations on the Company's results and activities have become less pronounced over the last few years, with the rise in sales of products such as savory flavors, functional food ingredients and natural extracts from medicinal plants, targeted for the pharmaceutical/ nutraceutical industry, which are less impacted by seasonal demand.

The acquisition of PTI, which specializes mainly in savory flavors and fine ingredients (including to the processed meat industry), where demand increases in the winter, is expected to bring about a certain change in Frutarom's seasonality, as PTI sales are highest in the fourth quarter and lower in the first quarter.

D. LIQUIDITY

Frutarom continues to create strong cash flow from operating activities, helping it to reduce its debt level and continue to make strategic acquisition, while maintaining a reasonable debt level. Total cash flow from operating activities in 2013 reached US$88.7 million, compared with US$91.2 million in 2012. Over Q4 of 2013, the Company achieved cash flow from operating activities of US$30.6 million, compared with US$28.6 million in Q4 2012. Frutarom continuously acts to maintain the appropriate optimal working capital level according to expected growth, while taking into account seasonality, availability of the various raw materials and their current and expected future prices.

E. SOURCES OF FINANCING

Sources of Equity

Frutarom's equity as of December 31, 2013 totaled US$521.1 million (53.7% of the balance sheet) compared with US$$445.2 million as of December 31, 2012 (57.6% of the balance sheet). The change derives from an increase in net profit and from translation differences of values of assets in subsidiaries having operational currency other than the dollar (in light of the strengthening of exchange rates of European currencies and the NIS against the dollar as of December 31, 2013 compared with December 31, 2012).

Long-Term Loans Including Current Maturities of Long Term Loans (Average)

Average long-term credit from banks provided to the Company in 2013 totaled US$133.0 million, compared with US$173.9 million in 2012.

Average long-term credit from banks provided to the Company in Q4 2013 totaled US$120.6 million, compared with US$178.2 million in 2012. The reduction derives from a change in the composition of the loan the Company took between short term loans and a long term loans.

Short-Term Loans Excluding Current Maturities of Long Term Loans (Average)

The average short-term credit from banks provided to the Company in 2013 came to US$51.8 million, compared with US$30.3 million in 2012.

The average short-term credit from banks provided to the Company in Q4 2013 came to US$84.9 million, compared with US$13.1 million during the corresponding quarter in 2012. The increase in the scope of credit is the result of an interim loan taken during the period for financing acquisitions. After the balance sheet date, the loan was replaced by a long term loan.

Frutarom's cash balances as at 31 December 2013 came to US$57.6 million and net debt balance stood at US$190.7 million.

Accounts Payable and Other Payable (Average)

In Q4 2013, the Company had accounts payable and other payables in the amount of US$101.6 million, compared with US$90.3 million in the same quarter last year. During Q4 2013, the Company granted credit of US$139.4 million to its customers, compared with US$113.6 million during the same period last year. The increase in accounts payable and other payables is mainly the result of suppliers and customers balances of recently acquired companies.

As detailed in this report with respect to the Company's financial status, its liquidity, the positive cash flow it generates from its operating activities and its sources of financing, and assuming no material adverse changes in its sales and/or profitability, the Company estimates that the cash flow it generates from current operations will enable the full repayment of its expected liabilities without the need for external financing sources.

EXPOSURE TO AND MANAGEMENT OF MARKET RISKS

The Group's activity is characterized by significant decentralization. Through its core business the Company produces thousands of products intended for thousands of customers throughout the world, using thousands of raw materials purchased from a wide range of suppliers worldwide. The Group is not significantly dependent on any one of its customers, products or suppliers.

A. RESPONSIBILITY FOR MARKET RISK MANAGEMENT

Mr. Alon Granot, Executive Vice President and CFO, is responsible for managing market risk. The Company's Management and Board of Directors are updated on material changes in the Company's exposure to various risks, and conduct discussions as needed.

For details about Mr. Alon Granot, see Regulation 26a in Chapter D to this report (Additional Details on the Corporation).

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 single supplier representing more than 5% of total raw material purchases. 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. The Company does not normally make future transactions and is exposed to price fluctuations in the raw materials it uses in accordance with global price trends. The Company's Executive Vice President for Global Supply Chain and Operations follows raw material prices on an ongoing basis.

Over the past few years there has been a continuing trend of substantial price increases for most of the raw materials Frutarom uses for the manufacture of its products. 2013 saw stabilization in price levels for most raw materials.

Currency Risks

The Company's sales worldwide are conducted in a number of currencies (mainly in Euro, US Dollars, Russian Ruble, Swiss Francs, Pounds Sterling and New Israeli Shekels). Therefore, there is sensitivity to fluctuations in the exchange rates. However, the fact that Frutarom's raw materials purchases are in fact conducted in various currencies reduces the exposure to currency fluctuation risks. Most of the non- US dollar monetary balances derive from the local activity of the Company's subsidiaries in Europe and in Israel. The functional currency of these companies is the local currency, and therefore the currency translation balances in the local currency of each of these companies does not influence the Group's finance expenses, and is directly attributed to a currency translation capital fund. Monetary balances in other currencies are attributed to financing expenses. Currency exposure is reviewed as necessary, and at least once every quarter. The Company does not generally take external hedging actions nor does it use other financial instruments for protection against currency fluctuations. For more details see Note 3A of the Company's financial statement of December 31, 2013, attached to this report.

Interest Risks

The Company's sources of banking finance, short- and long-term, are mainly quoted in Euro, US Dollar, Pound Sterling, Swiss Franc and NIS (according to the functional currency of the borrowing company), and bear variable Libor interest. The Company's policy is not to take protective steps against possible interest increases and there is therefore sensitivity to changes in interest rates. As of the balance sheet date, the Company does not hold any financial derivatives. As of December 31, 2013 the Company held long-term loans with the deduction of current maturities in an overall amount of US$140 million. The scope of its short-term debt, including current maturities of long-term loans, was US$108 million. The Company has cash flow reserves of US$57.6 million.

C. THE COMPANY'S POLICY REGARDING MARKET RISK MANAGEMENT

1. The Group's management conducts an ongoing evaluation of market risks in the area of raw material prices, currency rates and interest. Unusual occurrences such as acute currency devaluations in a target country, sharp changes in interest rates or price changes in important raw materials that could influence the Group's activity 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 management of market risks in the area of raw materials prices.

3. The Group's management attempts to reduce currency exposure, whether economic or accounting, by balancing liabilities and assets in each of the various currencies in which the Group operates. The Executive Vice President and CFO is responsible for the management of currency exposure in the Group. The Group typically takes loans in local currency with variable Libor interest.

4. The level of exposure is evaluated by the Group’s accounting department on a regular basis, discussed among the Group's management, allowing immediate response to any unusual developments in the various markets and level is not limited in advance by quantity. The exposure level is also reviewed by the Company's Board of Directors on an ad hoc basis.

5. During this report period, Frutarom did not use financial instruments or other instruments to protect itself from the market risks to which it is exposed.

In 2013, there were no changes to the Group’s 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 operations management on a regular basis and reported to the management as necessary. Discussions are held by the Company’s management once a period, addressing the implementation of risk management policy as it relates to raw materials prices, currency and interest. The Executive Vice President and CFO reports to the Board of Directors regarding exposure to these risks at least once a year and during times of extreme changes in the global economy, exchange rates, raw material prices, and interest rates.

E. LINKAGE BASES REPORT

CURRENCY EXPOSURE ACCORDING TO PRIMARY LINKAGE BASES AS AT DECEMBER 31, 2013

	US$	NIS	GBP	Euro	CHF	Ruble	Others	Total
	In US$ 000							
Assets								
Cash and cash equivalents	13,220	467	4,627	22,248	3,297	3,537	10,216	57,612
Customers	24,172	11,416	12,901	44,378	7,537	19,531	18,438	138,373
Other debtors	5,663	704	2,083	4,505	1,848	5,445	3,998	24,245
Inventory	42,302	-	20,883	39,113	20,496	21,775	10,152	154,721
Other long term debtors	47	-		3,492	-		-	3,539
Fixed assets, net	43,066	-	13,116	74,993	56,387	10,859	10,146	208,567
Other assets, net	130,305	-	53,111	139,843	2,998	37,854	19,618	383,729
Total assets	**258,775**	**12,587**	**106,721**	**328,572**	**92,563**	**99,001**	**72,564**	**970,786**
Liabilities								
Bank loans	151,677	-	13,854	44,313	36,497	-	1,998	248,339
Suppliers	9,730	5,845	5,715	25,812	4,467	2,966	3,872	58,407
Other creditors	9,337	8,162	6,890	12,319	6,905	5,210	3,940	52,763
Employee retirement rights liabilities	991	-	-	11,966	10,091		78	23,126
Deferred taxes	10,154	-	6,089	8,867	4,958	3,452	564	34,084
Other long term liabilities	7,348	-	-	-	-	24,410	1,250	33,008
Total liabilities	**189,237**	**14,007**	**32,548**	**103,277**	**62,918**	**36,038**	**11,702**	**449,727**
Equity capital								**521,059**
Net liabilities	**69,538**	**(1,420)**	**74,173**	**225,295**	**29,645**	**62,963**	**60,866**	**0**

F. SENSITIVITY TESTS

Sensitivity to Changes in the US Dollar- Israeli Shekel Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	**+10%**	**+5%**	**-**	**-5%**	**-10%**
Exchange rate	**3.818**	**3.645**	**3.471**	**3.297**	**3.124**
			US$ 000		
Cash and cash equivalents	(47)	(23)	467	23	47
Customers	(1,142)	(571)	11,416	571	1,142
Other debtors	(70)	(35)	704	35	70
Other long term debtors	(5)	(2)	47	2	5
	(1,264)	**(631)**	**12,634**	**631**	**1,264**
Credit from banking corporations	-	-	-	-	-
Suppliers and service providers	585	292	5,845	(292)	(585)
Other creditors	816	408	8,162	(408)	(816)
	1,401	**700**	**14,007**	**(700)**	**(1,401)**
Total exposure, net	**137**	**69**	**(1,373)**	**(69)**	**(137)**

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	**0.665**	**0.635**	**0.605**	**0.574**	**0.544**
			US$ 000		
Cash and cash equivalents	(463)	(231)	4,627	231	463
Customers	(1,290)	(645)	12,901	645	1,290
Other debtors	(131)	(66)	1,310	66	131
	(1,884)	**(942)**	**18,838**	**942**	**1,884**
Credit from banking corporations	1,385	693	13,854	(693)	(1,385)
Bank loans	572	286	5,715	(286)	(572)
Suppliers and service providers	689	345	6,880	(345)	(689)
Other creditors	**2,646**	**1,324**	**26,459**	**(1,324)**	**(2,646)**
Total exposure, net	**762**	**382**	**(7,621)**	**(382)**	**(762)**

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	**0.798**	**0.762**	**0.726**	**0.690**	**0.653**
			US$ 000		
Cash and cash equivalents	(2,225)	(1,112)	22,248	1,112	2,225
Customers	(4,438)	(2,219)	44,378	2,219	4,438
Other debtors	(341)	(170)	3,405	170	341
Other long term debtors	(7)	(3)	68	3	7
	(7,011)	**(3,504)**	**70,099**	**3,504**	**7,011**
Credit from banking corporations	4,431	2,216	44,313	(2,216)	(4,431)
Suppliers and service providers	2,581	1,291	25,812	(1,291)	(2,581)
Other creditors	1,232	616	12,319	(616)	(1,232)
	8,244	**4,123**	**82,444**	**(4,123)**	**(8,244)**
Total exposure, net	**1,233**	**619**	**(12,345)**	**(619)**	**(1,233)**

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	**0.980**	**0.935**	**0.891**	**0.846**	**0.802**
			US$ 000		
Cash and cash equivalents	(330)	(165)	3,297	165	330
Customers	(754)	(377)	7,537	377	754
Other debtors	(60)	(30)	596	30	60
	(1,144)	**(572)**	**11,430**	**572**	**1,144**
Credit from banking corporations	3,650	1,825	36,497	(1,825)	(3,650)
Suppliers and service providers	447	223	4,467	(223)	(447)
Other creditors	691	345	6,905	(345)	(691)
	4,788	**2,393**	**47,869**	**(2,393)**	**(4,788)**
Total exposure, net	**3,644**	**1,821**	**(36,439)**	**(1,821)**	**(3,644)**

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	**36.066**	**34.426**	**32.787**	**31.148**	**29.508**
			US$ 000		
Cash and cash equivalents	(354)	(177)	3,537	177	354
Customers	(1,953)	(977)	19,531	977	1,953
Other debtors	(201)	(100)	2,008	100	201
	(2,508)	**(1,254)**	**25,076**	**1,254**	**2,508**
Credit from banks	-	-	-	-	-
Suppliers and service providers	297	148	2,966	(148)	(297)
Other creditors	521	261	5,210	(261)	(521)
Other long term creditors	2,441	1,221	26,410	(1,221)	(2,441)
	3,259	**1,630**	**32,586**	**(1,630)**	**(3,259)**
Total exposure, net	**751**	**376**	**(7,510)**	**(376)**	**(751)**

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$ 000		
Cash and cash equivalents	(1,022)	(511)	10,216	511	1,022
Customers	(1,844)	(922)	18,438	920	1,844
Other debtors	(179)	(89)	1,789	88	179
	(3,045)	**(1,522)**	**30,443**	**1,522**	**3,045**
Credit from banks	200	100	1,998	(100)	(200)
Suppliers and service providers	387	194	3,872	(194)	(387)
Other creditors	394	197	3,940	(197)	(394)
Other long term creditors	125	63	1,250	(63)	(125)
	1,106	**554**	**11,060**	**(554)**	**(1,106)**
Total exposure, net	**(1,939)**	**(969)**	**19,383**	**969**	**1,939**

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$ 000				
Short Term Loans (Chinese Yuan)	11	5	1,804	(5)	(11)
Total exposure, net	**11**	**5**	**1,804**	**(5)**	**(11)**

F. SUMMARY OF SENSITIVITY TESTS TABLES

The functional currency of the majority of the Group's companies is the local currency in each company's respective country of residence; 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 shareholders' equity (currency translation capital fund).

Sensitivity to Changes in the US Dollar- Israeli Shekel Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	+10%	+5%	-	-5%	-10%
Exchange rate	3.818	3.645	3.471	3.297	3.124
	US$ 000				
Total Exposure net	**137**	**69**	**(1,373)**	**(69)**	**(137)**

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	0.665	0.635	0.605	0.574	0.544
	US$ 000				
Total Exposure net	**762**	**382**	**(7,621)**	**(382)**	**(762)**

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	0.798	0.762	0.726	0.690	0.653
	US$ 000				
Total exposure, net	**1,233**	**619**	**(12,345)**	**(619)**	**(1,233)**

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	0.980	0.935	0.891	0.846	0.802
	US$ 000				
Total exposure, net	**3,644**	**1,821**	**(36,439)**	**(1,821)**	**(3,644)**

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	36.066	34.426	32.787	31.148	29.508
	US$ 000				
Total exposure, net	**751**	**376**	**(7,510)**	**(376)**	**(751)**

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$ 000				
Total exposure, net	**(1,939)**	**(969)**	**19,383**	**969**	**1,939**

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$ 000				
Total exposure, net	**11**	**5**	**1,804**	**(5)**	**(11)**

CORPORATE GOVERNANCE ASPECTS

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 report (Additional Details 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.

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 Board of Directors' 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 level of complexity.

The Internal Auditor's Supervisor

The internal auditor reports to the Company Board of Directors' Audit Committee and to the President of the Company.

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 Board of Directors' 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 substantial 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 2013
Activity in Israel	211
Activity outside of Israel	983

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.

In 2013, the Internal Auditor's scope of services totaled 1,194 working-hours compared to 1,129 working-hours in 2012.

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.

Free Access to 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 conduct the audit.

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 2013, the Audit Committee held meetings which included discussions on the findings of the internal auditor, on January 10, 2013 and August 18, 2013. The members of the Company’s Audit Committee, the President of the Company, the Executive Vice President and CFO, the Executive Vice President for Global Supply Chain and Operations, the Global VP Legal and Corporate Secretary, the VP Finance and 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 per the request of the Chairmen of the Audit Committee.

Assessment by the Board of Directors of the Company 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 2013 was NIS 296.1 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 EXTERNAL 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 26% of the Company's total assets, and their revenue constitutes 31% 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 2013 totaled US$1,256 thousand (compared to US$1,200 thousand in 2012) in Israel and in the subsidiaries abroad (14,109 hours in 2013 compared to 14,251 hours in 2012). 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$143thousand in 2013 (compared to US$78 thousand in 2012) 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. DISCLOSURE REGARDING THE APPROVAL PROCESS OF THE FINANCIAL REPORTS

The Company's financial reports are submitted for approval to the Board of Directors, the Company's overall supervising body, a few days after the Board of Directors' committee for the review of the financial reports (the "**Balance Sheet Committee**") has discussed the financial reports 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 report (Further Details on the Corporation)

Members of the Balance Sheet Committee

The members of the Balance Sheet Committee are the members of the Audit Committee – Mr. Yacov Elinav, External Director and the chairman of the committee, Mr. Isaac Angel, External Director, and Mr. Gil Leidner, Director. The Balance Sheet Committee members have financial and accounting expertise and ability to read financial reports and provided the Company with a written declaration in this regard. 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 report (Additional Details on the Corporation).

Balance Sheet Committee Process 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 16, 2014. The members of the committee received the 2013 financial reports 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 and CEO, Mr. Ori Yehudai, the Executive Vice President and CFO, Mr. Alon Granot, the Vice President of Finance, Mr. Guy Gill, and

Ms. Tali Mirsky, Global Vice President Legal Affairs and Company Secretary. At the meeting, the Balance Sheet Committee discussed, 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 recommendations of the committee were delivered to the Company's Board of Directors two business days before the Board's meeting at which the financial reports were discussed. The Board of Directors considered the said time period reasonable in light of the scope and complexity of the recommendations.

<u>Board of Directors' Report Approval Procedure</u>

The members of the Board of Directors receive the draft financial reports several days before the date of the Board meeting at which the reports are brought for their approval. The Company's Independent auditors and members of the Company's senior management are also invited to attend the meeting, including Mr. Ori Yehudai, the President and CEO, Mr. Alon Granot, Executive Vice President and CFO, Mr. Amos Anatot, Executive Vice President and COO Global Supply Chain, Mr. Guy Gill, Vice President of Finance, and Ms. Tali Mirsky, Global Vice President of Legal Affairs and Corporate Secretary or another of the Company's legal counsel. Mr. Yoav Barak, the Company's internal auditor, is also invited to the meeting. During the meeting, the Board of Directors discusses the recommendations of the Balance Sheet Committee regarding the financial reports. The President and CEO and Executive Vice President and CFO also present the Group's business and financial results for the relevant period in comparison to previous periods to the Board of Directors at this meeting, with emphasis on special events that occurred during the period. During the presentation of the Group's results, members of the Company's management answer questions and relate to the Directors' comments. Following presentation of the Company's financial results, the Company's independent auditors answer the Directors' questions. Finally, the Board of Directors votes on approval of the financial reports. All of the members of the Board of Directors were present at the Board meeting held on March 18, 2014, and the financial reports for 2013 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 reports on the matter dated December 29, 2013.

(2) On March 18, 2014 the Company's Board of Directors, after approval by the Compensation Committee of the Board of Directors (the "**Compensation Committee**") from March 16, 2014, resolved on bonuses for senior office holders in the Company for 2013 (except the bonus for the President and CEO of the Company, as detailed in section 5 below). As the Company has adopted a compensation policy under amendment 20 to the Companies Law 1999 ("**Amendment 20"**), on January 14, 2014, the bonuses for 2013 were approved according to the criteria which have served the Company in resolving on bonuses prior to the enactment of Amendment 20, other relevant criteria under the provisions of Amendment 20 and in accordance with the thresholds and ceilings prescribed in the compensation policy, all as set forth in section 4 below. The bonuses were approved after a detailed discussion held by the compensation Committee and the Board of Directors with regard to each office holder separately.

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 18, 2014.

(3) Prior to the discussion on the remuneration of senior officeholders, the members of the Board of Directors were presented with all relevant data for each senior officeholder as required by regulations 21 and 22 of the Securities Regulations (Immediate and Periodic Reports), 1979 and by the provisions of sections B and C to the sixth addendum to these regulations, and other relevant data needed in order to resolve on the matter of the compensation, its components, fairness and reasonableness, including (A) financial data regarding the last year and previous years, data from previous years regarding the Company's profitability and the amounts of bonuses paid in the Company, the overall compensation paid to each of the relevant senior office holders including all components thereof, terms of existing agreements for each senior office holder; (B) each office holder's capabilities, achievements and contributions to the Company; (C) the recommendations of the Company's President regarding compensation for each senior office holder serving under him (D) comparative data regarding compensation paid to senior office holders in comparable positions in other public companies in Israel with of a similar scope and nature to those of the Company; and (E) data regarding average and median wages of Company employees. The Compensation Committee and Board of Directors were provided with a survey regarding this data during the course of the meeting.

(4) In determining the amount of the bonuses (other than the bonus for the President and CEO of the Company, as detailed in section 5 below) the Compensation Committee and the Board of Directors took into account, inter alia, the following parameters: (a) the business and financial performance of the Group, its size, scope and nature of activity, the profit, profit margins and rate of growth achieved; (b) each senior office holders' contribution to these achievements, the economic value of

services rendered by each one to the Group, the scope of office, tasks, existing employment agreement, areas of responsibility and each senior office holder's satisfaction of requirements of the position he holds; (c) the Company's business goals; (d) professional experience and achievements of each senior office holder, education, skills and expected contributions to the Company; (e) customary terms of wages in the Company, the relation between the senior office holder's terms of employment and the average and median wages of other Company employees, and the effect of any the gaps between these on work relations in the Company. The Compensation Committee and the Board of Directors also took into account the Company's growth rate over the year, successful realization of the latest strategic acquisitions and the integration of such, and the fact of the Company's status as one of the leading companies in the world in its field, as well as considerations regarding promotion of the Company's goals, its work plans and policies and creating proper incentives for Company office holders, taking into account the long term and according to the office holders position. As stated, no goals were determined in advance for the purpose of considering bonuses, however, in determining the amount of bonuses, members of the Compensation Committee and of the Board of Directors took into consideration thresholds and ceilings prescribed in the Company's compensation policy.

(5) The Board of Directors in its meeting of March 18, 2014 also discussed compensation for senior office holders under the provisions of regulation 10(b)(4) to the Securities Regulations (Periodic and Immediate Reports) 1970. The Board of Directors resolved, after a detailed discussion held with regard to each office holder separately, that the compensation granted to each one was in line with the Company's compensation policy and was fair and reasonable in light of the size and complexity of the Group, its business achievements over the last few years, tasks and scope of responsibility of each one of the senior office holders in the Group and each one's contribution to the achievements and economic value of the services provided to the Group by each one of the senior office holders.

(6) On December 6, 2012, the Board of Directors approved formalization of the annual bonus for the Company's President and CEO (the President), as part of his existing terms of employment, after approval of the Company's Audit Committee sitting as the Compensation Committee, on December 4, 2012. For further details regarding formalization of the President's bonus, the method of determination and reasoning, see the Company's report dated June 27, 2013.

DISCLOSURE RELATING TO THE CORPORATE FINANCIAL REPORTING

A. DIVIDEND DISTRIBUTION IN 2013

On March 12, 2013, the Company's Board of Directors resolved to approve a distribution of a cash dividend in the amount of NIS 0.24 per share. On May 6, 2013, a dividend in the total amount of US$3,892 thousand was paid out.

B. OCCURRENCES FOLLOWING THE DATE OF THE REPORT ON THE FINANCIAL STATUS WHICH ARE MENTIONED IN THE FINANCIAL REPORT

On March 18, 2014, concurrently with the approval of the financial statements of December 31, 2013, the Company's Board of Directors resolved on the distribution of a dividend in the amount of NIS 0.28 per share, in a total amount of NIS 16,382 thousand (US$4,732 thousand).

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 reports dated December 31, 2013, 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 rate of discount is determined by external actuaries at the end of each year. This rate of discount is used in determining the estimated updated value of the future cash flows that would be required to cover 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 possibility of determining the required rate based on the interest rates applicable to government bonds denominated in the currency in which the benefits will be paid having maturity periods approximating to the periods of the related liabilities will be considered.

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 in Respect of Goodwill and Intangibles

Once per year, the Company reviews the need to provide for impairment of goodwill and intangibles. The need to make such a provision is assessed in relation 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 REPORT UNDER REGULATION 9(C) OF THE REGULATIONS

The Company in its 2013 Annual Report, did not include a separate financial report as set forth in Regulation 9C of the Regulations (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 reports.

The Company's decision that the information is negligible is based on 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 financing 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. Its only balances are 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 Regulation 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 Regulation 10(14) of the Regulations and found that they do not exist.

The Board of Directors of the Company held five meetings during 2013.

The Board of Directors thanks Frutarom's employees and management for the Company's fine achievements.

Dr. John J. Farber
Chairman of the Board

Ori Yehudai
President & CEO

March 18, 2014

CHAPTER C

FINANCIAL REPORTS

FRUTAROM INDUSTRIES LTD.

2013 FINANCIAL STATEMENTS

FRUTAROM INDUSTRIES LTD.

2013 FINANCIAL STATEMENTS

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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, 2013. 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").

As indicated in the assessment of effectiveness of internal control components of the Board of Directors and management, this assessment does not apply to components of internal control over financial reporting of Protein Technologies Ingredients ("PTI"), which was acquired on November 18, 2013 and whose the assets and revenue included in consolidation constitute 6% and 5%, respectively, of total assets and revenues in the consolidated financial statements as of December 31, 2013 and for the year ended on that date. Accordingly, our audit did not apply to internal control components over financial reporting of PTI.

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.

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, 2013.

Kesselman & Kesselman, 1 Nathanson Street, Haifa 33034, Israel, P.O Box 33984, Haifa 31339
Telephone: +972 -4- 8605000, Fax:+972 -4- 8605001, www.pwc.co.il

REPORT OF THE AUDITORS (continued)

We also audited, the Company's financial statements as of December 31, 2013 and 2012 and for each of the three years in the period ended December 31, 2013, in accordance with generally accepted auditing standards, and our report, of March 18, 2014 included an unqualified opinion on these financial statements.

Haifa, Israel 18, March, 2014	Kesselman & Kesselman Certified Public Accountants (lsr.) A member firm of International PricewaterhouseCoopers Limited

pwc

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, 2013 and 2012 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, 2013. 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 26% and 21% of total consolidated assets as of December 31, 2013 and 2012, and whose revenues included in consolidation constitute approximately 31%, 26%, and 14% of total consolidated revenues for each of the three years in the period ended December 31, 2013. 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, 2013 and 2012 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, 2013, 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, 2013, and our report in March 18, 2014 included an unqualified opinion on the effectiveness of those components.

Haifa, Israel	Kesselman & Kesselman
18, March, 2014	Certified Public Accountants (lsr.)
	A member firm of International PricewaterhouseCoopers Limited

FRUTAROM INDUSTRIES LTD.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

	Note	2013	2012
		As of 31 December	
		U.S. dollars in thousands	
Assets			
CURRENT ASSETS:			
Cash and cash equivalents	18	57,612	53,933
Accounts receivable:	15		
Trade		138,373	106,754
Other		12,442	10,949
Prepaid expenses and advances to suppliers		11,803	6,966
Inventories	16	154,721	122,433
		374,951	301,035
NON-CURRENT ASSETS :			
Property, plant and equipment – net	7	208,567	188,824
Intangible assets – net	2f,8	383,729	279,198
Deferred income tax assets	13d	3,424	3,075
Other	17	115	277
		595,835	471,374
Total assets		970,786	772,409

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 18, 2014.

	Note	As of 31 December 2013	2012
		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	108,226	52,196
Accounts payable:	19		
Trade		58,407	48,237
Other		52,763	39,269
		219,396	139,702
NON-CURRENT LIABILITIES:			
Long-term loans net of current maturities	9	140,113	137,836
Retirement benefit obligations, net	10	23,126	*24,329
Deferred income tax liabilities	13d	34,084	*24,420
Liability for put option for the shareholders of a subsidiary	5j	27,522	-
Other	5	5,486	892
		230,331	187,477
COMMITMENTS AND CONTINGENT LIABILITIES	11		
Total liabilities		449,727	327,179
EQUITY:	12		
EQUITY ATTRIBUTED TO OWNERS OF THE PARENT COMPANY:			
Ordinary shares		16,781	16,713
Other capital surplus		104,293	102,099
Translation differences	2c	27,296	16,749
Retained earnings		371,867	*310,477
Less - cost of Company shares held by the company and by subsidiary		(1,981)	(3,043)
Non-controlling interest		2,803	2,235
Total equity		521,059	445,230
Total equity and liabilities		970,786	772,409

*Restated, see note 2x.

The accompanying notes are an integral part of these financial statements.

FRUTAROM INDUSTRIES LTD.

CONSOLIDATED INCOME STATEMENTS

	Note	2013	2012	2011
		Year ended 31 December		
		U.S. dollars in thousands, (except for per share data)		
SALES		673,693	618,001	518,443
COST OF SALES	20a	416,897	391,742	329,866
GROSS PROFIT		256,796	226,259	188,577
Selling, marketing, research and development expenses - net	20b	115,223	104,932	88,641
General and administrative expenses	20c	52,131	49,197	39,231
Other expenses (income) - net	20d	2,685	(718)	2,041
INCOME FROM OPERATIONS		86,757	72,848	58,664
FINANCIAL EXPENSES (INCOME) – net	20e	7,528	7,240	5,798
INCOME BEFORE TAXES ON INCOME		79,229	65,608	52,866
INCOME TAX	13e	15,608	13,628	10,835
NET INCOME FOR THE YEAR		63,621	51,980	42,031
PROFIT ATTRIBUTED TO:				
Owners of the parent company	5j	63,129	51,570	42,031
Non-controlling interest		492	410	-
		63,621	51,980	42,031
		U.S dollars		
EARNINGS PER SHARE:	2v			
Basic		1.09	0.90	0.73
Fully diluted		1.08	0.90	0.73

The accompanying notes are an integral part of these financial statements.

FRUTAROM INDUSTRIES LTD.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Year ended 31 December		
	2013	**2012**	**2011**
	U.S. dollars in thousands		
Income for the year	63,621	51,980	42,031
Other comprehensive income:			
Items that will not be reclassified subsequently to profit or loss:			
Remeasurement of net defined benefit Liability, net after tax	2,153	*(4,756)	*18
Items that could be reclassified subsequently to profit or loss:			
Translation differences	10,622	4,393	(5,255)
Total comprehensive income for the Year	76,396	51,617	36,794
Attributable to:			
Owners of the parent company	75,829	51,207	36,794
Non-controlling interest	567	410	-
Total	76,396	51,617	36,794

*Restated, see note 2x

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 subsidiary	Total
		U.S. dollars in thousands					
BALANCE AT 1 JANUARY 2011		16,597	96,630	17,611	*228,023	(2,661)	356,200
Comprehensive income:							
Income for the year		-	-	-	42,031	-	42,031
Other comprehensive income	2c	-	-	(5,255)	18	-	(5,237)
Total comprehensive income for the year		-	-	(5,255)	42,049	-	36,794
Plan for allotment of Company shares to employees of subsidiary:	2r						
Purchase of Company shares by subsidiary		-	-	-	-	(892)	(892)
Receipts in respect of allotment of Company shares to employees	12b	-	(382)	-	-	572	190
Allotment of shares and options to senior employees-	12b						
Recognition of compensation related to employee stock and option grants		-	1,108	-	-	-	1,108
Dividend paid	12c	-	-	-	(3,380)	-	(3,380)
		-	726	-	(3,380)	(320)	(2,974)
BALANCE AT 31 DECEMBER 2011		16,597	97,356	12,356	266,692	(2,981)	390,020

*Restated, see note 2x

FRUTAROM INDUSTRIES LTD.

CONSODLIATED STATEMENTS OF CHANGES IN EQUITY

	Note	EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT							
		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
		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

*Restated, see note 2x

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	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 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

*Restated, see note 2x

The accompanying notes are an integral part of these financial statements.

FRUTAROM INDUSTRIES LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Note	2013	2012	2011
		Year ended 31 December		
		U.S. dollars in thousands		
CASH FLOWS FROM OPERATING ACTIVITIES:				
Cash generated from operations (see Appendix)		98,493	104,774	47,363
Income tax paid - net		(9,802)	(13,563)	(11,788)
Net cash provided by operating activities		88,691	91,211	35,575
CASH FLOWS FROM INVESTING ACTIVITIES:				
Purchase of property, plant and equipment		(20,111)	(12,558)	(7,835)
Purchase of intangibles		(868)	(2,284)	(2,564)
Interest received		276	195	642
Acquisition of subsidiaries - net of cash acquired	5	(114,620)	(75,280)	(57,963)
Acquisition of operations	5	-	-	(43,698)
Reimbursement in respect of acquisition of operation	5	-	-	3,850
Proceeds from sale of property		264	271	289
Net cash used in investing activities		(135,059)	(89,656)	(107,279)
CASH FLOWS FROM FINANCING ACTIVITIES:				
Dividend paid to the non-controlling interests in subsidiary		(97)	-	-
Receipts from senior employees in respect of allotment of shares		2,028	4,152	-
Interest paid		(3,456)	(5,553)	(2,207)
Receipt of long-term bank loans		45,693	131,231	102,002
Repayment of long-term bank loans		(41,750)	(116,802)	(40,064)
Receipt (discharge of short-term bank loans and credit - net		52,809	7,319	8,201
Purchase of Company shares by subsidiary – net of receipts in respect of the Shares		(214)	(908)	(702)
Dividend paid		(3,892)	(3,029)	(3,380)
Net cash provided by financing activities		51,121	16,410	63,850
INCREASE (DECREASE) IN CASH, CASH EQUIVALENTS AND BANK CREDIT		4,753	17,965	(7,854)
Balance of cash and cash equivalents and bank credit at beginning of year		53,933	36,472	44,389
Profits (losses) from exchange differences on cash, cash equivalents and bank credit		(1,074)	(504)	(63)
BALANCE OF CASH, CASH EQUIVALENTS AND BANK CREIDT AT END OF YEAR		57,612	53,933	36,472

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		
	2013	**2012**	**2011**
	U.S. dollars in thousands		
Cash generated from operations:			
Income before tax	79,229	65,608	52,866
Adjustments required to reflect the cash flows from operating activities:			
Depreciation and amortization	27,693	26,012	20,612
Recognition of compensation related to employee stock and option grants	1,510	1,553	1,108
Liability for employee rights upon retirement - net	166	(655)	225
Loss (gain) from sale and write-off of fixed assets and other assets	(150)	92	17
Erosion of loans	1,212	1,003	-
Interest paid - net	3,180	5,358	1,565
Loss from change in fair value of financial instruments	-	289	-
Income from bargain purchase	-	(1,729)	-
	33,611	31,923	23,527
Operating changes in working capital:			
Decrease (increase) in accounts receivable:			
Trade	(8,966)	(1,712)	(12,035)
Other	(848)	(206)	(3,046)
Decrease in other long-term receivables	258	136	-
Increase (decrease) in accounts payable:			
Trade	3,432	1,506	8,342
Other	(2,999)	3,772	(5,495)
(decrease) in other long-term payables	(117)	(379)	-
Decrease (increase) in inventories	(5,107)	4,126	(16,796)
	(14,347)	7,243	(29,030)
Cash flows from operating activities	98,493	104,774	47,363

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 145 countries to more than 15,500 clients. The Group has production facilities in Europe, North America, Latin America, Israel and Asia (see also a list of subsidiaries in Note 23); The group has 38 research and development laboratories and it sells and markets its products principally through its 69 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 2013 and 2012 and for each of the three years in the period ended 31 December 2013, 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

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are immediately exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date the 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:					
2013	3.47	0.60	0.73	0.89	32.79
2012	3.73	0.62	0.76	0.92	30.44
2011	3.82	0.65	0.77	0.94	32.08
Increase (decrease) of the dollar: during the year	%	%	%	%	%
2013	(7.0)	(2.2)	(4.3)	(2.8)	7.7
2012	(2.3)	(4.6)	(1.9)	(2.7)	(5.1)
2011	7.7	0.4	3.3	0.4	5.1

	NIS	**Pound Sterling**	**Euro**	**Swiss Franc**	**Ruble**
Average exchange rate during the year:					
2013	3.61	0.64	0.75	0.93	31.84
2012	3.86	0.63	0.78	0.94	30.99
2011	3.58	0.62	0.72	0.89	29.33
Increase (decrease) during of the dollar during the year:	%	%	%	%	
2013	(6.3)	1.3	(3.3)	(1.2)	2.7
2012	7.8	1.2	8.3	5.9	5.7
2011	(4.2)	(3.6)	(4.6)	(14.5)	(3.2)

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	10

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.

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 category: 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.

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):

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

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 Group receives services from employees as consideration for equity instruments (options) of Group companies. The fair value of the employee services received in exchange for the grant of the options is recognized as an expense in the statement of income. The total amount to be expensed is determined by reference to the fair value of the options granted:

- considering the impact of any non-market vesting conditions (for example, remaining an employee of the entity over a specified time period); and
- excluding the impact of any non-vesting conditions.

Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. The total expense is recognized over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the date of each statement of financial position, the Group revises its estimates of the number of options that are expected to vest based on the non-marketing vesting conditions. It recognizes the impact of the revision to original estimates, if any, in the statement of income, with a corresponding adjustment to equity.

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:		
2013	57,976	58,559
2012	57,344	57,613
2011	57,265	57,475

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, 2013:

a) IAS 19 – "Employee Benefits" (Amended 2011) (hereafter – the revised IAS 19)

Commencing January 1, 2013, the group applies the revised IAS 19 for the first time.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

The first time application was made retrospectively. Therefore, comparative financial information is restated.

The revised IAS 19, "Employee benefits", introduces significant changes to the recognition and measurement of defined benefit pension expense and termination benefits, and to the disclosures for all types of employee benefits. The key changes are as follows:

- Actuarial gains and losses" are renamed "remeasurements of the defined benefit liability (asset)" (hereinafter - remeasurements), which includes in addition to actuarial gains and losses, certain elements defined in the revised IAS 19. Remeasurements are immediately recognized in "other comprehensive income" (OCI). This eliminates the option for recognition of actuarial gains and losses in profit or loss and also eliminates the option to use of the corridor approach.
- Past-service costs will be recognized immediately in the period no longer be spread over a future-service period to vesting.
- Expense for a funded benefit plan will include net interest expense or income, calculated by applying the discount rate currently used under IAS 19 to the net defined benefit asset or liability. This will replace the "finance charge" and "expected return on plan assets" methods as used in the previous version of IAS 19.
- The distinction between short- and long-term benefits for measurement purposes is based on when payment is expected, not when payment can be demanded.
- Any benefit that has a future-service obligation is not a termination benefit. A liability for a termination benefit is recognized when the entity can no longer withdraw the offer of the termination benefit or recognizes any related restructuring costs.
- There are additional disclosure requirements compared with IAS 19 in its previous version.

Until the first time application of the revised IAS 19, the accounting policy of the Group was to recognize actuarial gains or losses arising from changes in actuarial assumptions and from the difference between past assumptions and actual results, by the amount these gains or losses exceed the higher of 10% of the present value of the defined benefit liability and 10% of the fair value of plan assets. These gains or losses were carried to income over the expected average term of employment. Subsequent to application of the revised IAS 19, the Group does not defer the recognition of re-measurements. The "re-measurements", as recomputed in accordance with the new provisions, are fully carried to other comprehensive income in the period in which they have arisen. The first time application of IAS 19 did not have a material effect on the consolidated financial statements of the Group.

b) IFRS 12 – "Disclosure of Interests in Other Entities" (hereafter – IFRS 12)

IFRS 12 prescribes the disclosure requirements relating to the accounting issues accounted for in accordance with IFRS 10 and IFRS 11 and replaces the currently applicable disclosure requirements pursuant to IAS 28 and IAS 27.
The disclosure requirements provided in IFRS 12 refer to the following issues: Significant judgments and discounts, rights in subsidiaries, rights in joint arrangements and in associates, and rights in structured entities that have not been consolidated within the financial statements.

The Group applied IFRS 12 for the first time commencing January 1, 2013.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):

The first time application of IFRS 12 did not have a material effect on the consolidated financial statements of the Group.

c) IFRS 13 – "Fair Value Measurement" (hereafter – "IFRS 13")

IFRS 13, 'Fair value measurement', aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs. The requirements do not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards within IFRSs.

The Group applied IFRS 13 for the first time commencing January 1, 2013. The standard was applied prospectively. It is not required to apply the disclosure requirements of IFRS 13 to comparative information for periods before the first time application of IFRS 13. The first time application of IFRS 13 did not have a material impact on the measurement of items in the consolidated financial statements of the Group.

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.

NOTE 3 – FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued):

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.
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 2013, 2012 and 2011, 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 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)	*

	31 December 2011			
	U.S. dollars in thousands			
	NIS	**Pound sterling**	**Euro**	**Swiss Franc**
Financial asset(liabilities), net	9,643	(12)	7,494	62
Gain (loss) from change:				
Impact of 1% weakening	(77)	*	(60)	*
Impact 1% strengthening	77	*	60	*

* Represents amounts lower than $1 thousand.

NOTE 3 – FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued):

2) Linkage of Monetary Balances

Monetary balances denominated in various currencies included in the Company's consolidated statement of financial position at 31 December 2013, are summarized below:

	US dollar	NIS	Pound Sterling	Euro	Swiss Francs	Ruble	Other currencies	Total
	U.S. dollars in thousands							
Assets:								
Current assets:								
Cash and cash equivalents	13,220	467	4,627	22,248	3,297	3,537	10,216	57,612
Accounts receivable:								
Trade	24,172	11,416	12,901	44,378	7,537	19,531	18,438	138,373
Other	2,630	704	1,310	3,405	596	2,008	1,789	12,442
Non-current assets - others	-	47	-	68	-	-	-	115
	40,022	12,634	18,838	70,099	11,430	25,076	30,443	208,542
Liabilities:								
Current liabilities:								
Short-term bank borrowings and loans	61,677	-	41	8,016	-	-	1,814	71,548
Accounts payable:								
Trade	9,730	5,845	5,715	25,812	4,467	2,966	3,872	58,407
Other	9,337	8,162	6,890	12,319	6,905	5,210	3,940	52,763
Non-current liabilities:								
Long-term loans	90,000	-	13,813	36,297	36,497	-	184	176,791
Other long-term payables	7,348	-	-	-	-	24,410	1,250	33,008
	178,092	14,007	26,459	82,444	47,869	32,586	11,060	392,517

Some of the balances are includes in the statements of financial position of the consolidated companies in the UK, EU, Switzerland, china, Brazil and Russia whose functional currencies are the Pound Sterling, the Euro, the Swiss Franc, Yuan, Brazilian Real and the Ruble, respectively, and therefore do not involve exposure to income and loss.

NOTE 3 – FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued):

2) Linkage of Monetary Balances

Monetary balances denominated in various currencies included in the Company's consolidated statement of financial position at 31 December 2012, are summarized below:

	US dollar	NIS	Pound Sterling	Euro	Swiss Francs	Other currencies	Total
	U.S. dollars in thousands						
Assets:							
Current assets:							
Cash and cash equivalents	18,157	1,008	2,953	19,046	3,533	9,236	53,933
Accounts receivable:							
Trade	18,663	10,644	12,695	42,429	7,030	15,293	106,754
Other	623	818	948	7,193	815	552	10,949
Non-current assets - others	-	60	-	217	-	-	277
	37,443	12,530	16,596	68,885	11,378	25,081	171,913
Liabilities:							
Current liabilities:							
Short-term bank borrowings and loans	-	5,893	55	4,946	-	1,450	12,344
Accounts payable:							
Trade	14,183	2,841	3,350	20,639	4,829	2,395	48,237
Other	4,138	7,449	7,211	10,697	6,633	3,141	39,269
Non-current liabilities:							
Long-term loans	53,552	-	22,639	55,310	46,177	10	177,688
Other long-term payables	-	-				892	892
	71,873	16,183	33,255	91,592	57,639	7,888	278,430

Some of the balances are includes in the statements of financial position of the consolidated companies in the UK, EU, Switzerland, China and Brazil whose functional currencies are the Pound Sterling, the Euro, the Swiss Franc, Yuan and the Brazilian Real, respectively, and therefore do not involve exposure to income and loss.

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 2013 of a 0.1% shift in interest rate on loans would have been a change of $ 171 thousand (2012 - $ 124 thousand; 2011 - $79 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.

NOTE 3 – FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued):

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.

The table presented below classifies the Group's financial liabilities into relevant maturity groupings based on the remaining period at 31 December 2013 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 2013:			
Borrowings	111,049	139,769	13,465
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
As of 31 December 2012:			
Borrowings	55,306	105,666	35,342
Accounts payable and accruals	87,506	940	-
	142,812	106,606	35,342

d) **Level 3 financial instrument –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 5j.

As of December 31, 2013, the amount of the option amounted to $ 27,522 thousands; the value of the option 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. 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 option the company used PTI's business plan which was prepared as part of the purchase transaction.

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 2013 and 2012 were as follows:

	2013	2012
	U.S. dollars in thousands	
Total borrowings (Note 9)	248,339	190,032
Less - cash and cash equivalents (Note 18)	(57,612)	(53,933)
Net debt	190,727	136,099
Total equity	521,059	445,230
Total capital	711,786	581,329
Gearing ratio	26.8%	23.4%

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 the operations of Rieber & Son ASA

On February 1, 2011 the Group acquired through a Norwegian subsidiary the industrial savory business of Rieber & Son ASA (hereafter – Rieber).
The Rieber operations include developing, producing and marketing savory flavoring solutions, including flavoring extracts, spice blends and other functional raw materials for the food industry, especially for the processed meat and seafood industry and the convenience food market. The Rieber operations has a broad customer base, including some leading food producers, especially in Scandinavia.

The cost of acquisition presented in the finanical statements amounts to 24,540 thousands Norwegian Krones ($ 4,279 thousands); the acquisition was financed by self funds.

The cost of acquisition was fully allocated to intangible assets which were acquired based on their fair value at the time of the acquisition.

The product formulas and customer relations are amortized over economic life of 20 years and 10 years respectively. The goodwill is not amortized but rather tested at least once a year for impairment.

NOTE 5 – BUSINESS COMBINATIONS (continued):

Set forth below are the assets and liabilities of Rieber at date of acquisition:

	Fair value
	U.S. dollars In thousands
Non-current assets -	
Intangible assets:	
Goodwill	3,540
Product formulas	373
Customer relations	366
	4,279

b. Acquisition of the operations of East Anglian Food Ingredients Ltd.:

On January 31, 2011, the Group acquired through a UK subsidiary the operations of the UK Company East Anglian Food Ingredients Ltd ("EAFI").

EAFI is engaged in development, production and marketing of savory flavoring solution, included flavoring extracts, spice blends and other functional raw materials for the food industry, focusing on convenience food, snacks and processed meat and fish. EAFI has a development, production and marketing site in the UK and a broad customer base.

The cost of acquisition presented in these financial statements amounts to $ 4,834 thousands (£ 3,000 thousands); the acquisition was funded from self funds.

The cost of acquisition was fully allocated to acquire tangible assets, intangible assets and liabilities which were acquired based on their fair value at the time of the acquisition.

The intangible assets that were recognized include: product formulas in the total amount of £ 146 thousands ($ 235 thousands), amortized over economic life of 20 years.
The acquired operations were merged to the existing operations of the subsidiary in U.K.

Assets and liabilities of EAFI at date of acquisition:

	Fair value
	U.S. dollars in thousands
Current assets:	
Accounts receivable:	
Trade	1,072
Inventory	1,909
Non-current assets:	
Fixed assets	2,438
Intangible assets	
Product formulas	235
Current liabilities :	
Accounts payable and accruals-trade	(693)
Deferred income taxes	(127)
	4,834

NOTE 5 – BUSINESS COMBINATIONS (continued):

c. Acquisition of the savory business of Christian Hansen Italia S.P.A:

On 26 May 2011, the Group signed, through a UK subsidiary, an agreement to acquire assets and savory operations of Christian Hansen ITALIA S.p.a ("CH"). On 29 July 2011, the transaction was closed.

The Savory operation of CH (the "acquired operation") develops, produces and markets innovative savory solutions (the non-sweet taste spectrum) including flavors, seasoning compounds and functional ingredients for the food industry, with special emphasis on processed meat and convenience food applications. The acquired operation has an extensive customer base comprised mainly of leading Italian meat processors. The activity also enjoys export sales in Russia, Ukraine, Poland, the Czech Republic and France. Included among the assets purchased is a state-of-the-art, high-capacity plant located in Parma, Italy that will enable Frutarom to grow its activities and to take advantage of operational synergies with its existing savory activities in Europe. The Acquired Activity also has advanced R&D laboratories.

The Acquired operation is highly synergetic with the activity of the German companies Gewurzmuller and Nesse (acquired by Frutarom in 2007 and 2006 respectively), the German Savory Functional Systems activity of Chr. Hansen (acquired in 2009) along with the acquisitions of EAFI and Rieber completed in early 2011.

Net acquisition cost presented in these financial statements amounts to $ 34,585 thousands (Total of € 23,972 thousands and includes a payment of € 25,000 thousands net of a refund of € 1,028 thousands received from the sellers in accordance with the adjustments mechanisms set in the acquisition agreement). The acquisition was financed using long-term bank credit.

The Group merged the marketing, finance, R&D and purchasing activities of the acquired operations with its existing operations.
The cost of acquisition was fully allocated to acquire tangible assets, intangible assets and liabilities based on their fair value on the date of acquisition.

The intangible assets that were recognized include: product formulas in the total amount of €3,118 thousands ($ 4,498 thousands), customer relations of € 4,034 thousands ($ 5,820 thousands) and goodwill of € 6,604 thousands ($ 9,527 thousands).

NOTE 5 – BUSINESS COMBINATIONS (continued):

Assets and liabilities of CH at the date of acquisition:

	Fair value
	U.S. dollars in thousands
Current assets:	
Accounts receivable:	
Inventory	4,112
Non-current assets:	
Deferred income taxes	550
Property, plant and equipment	13,023
Intangible assets	
Goodwill	9,527
Product formulas	4,498
Customer relations	5,820
Current liabilities :	
Accounts payable and accruals	
Others	(868)
Non-current liabilities :	
Long-term loans	(1,845)
Retirement benefit obligations, net	(232)
	34,585

d. Acquisition of Aromco Ltd.:

On 19 August 2011, the Group acquired thorugh a UK subsidiary 100% of share capital of a UK company – Aromco Ltd. ("Aromco").

Aromco develops, manufactures, and markets flavors for the food and beverage industry. Aromco is active mainly in the UK and in developing markets with high growth potential in Eastern Europe, Africa and Asia. Aromco operates a factory in Hertfordshire, England.

The Acquired operation is highly synergetic with Groups flavors activity. The Group merge Aromco's activity into its UK activity and global operations, realizing synergies.

The cost of acquisition presented in these financial statements amounts to $24,614 thousand (£ 15,000 thousand). The acquisition was financed by a long-term bank loan.

The cost of acquisition was allocated to acquired tangible assets, intangible assets and liabilities at their fair value on the date of acquisition.

The intangible assets that were recognized include: product formulas at $3,354 thousand (£ 2,044 thousand), customer relations at $4,750 thousand (£ 2,895 thousand) and goodwill at $16,127 thousand (£ 9,828 thousand).

NOTE 5 – BUSINESS COMBINATIONS (continued):

Assets and liabilities of Aromco at the date of acquisition:

	Fair value U.S. dollars in thousands
Current assets:	
Cash and cash equivalents	1,434
Accounts receivable:	
Trade	2,790
Inventory	1,058
Others	53
Non-current assets:	
Property, plant and equipment	530
Intangible assets:	
Product formulas	3,354
Customer relations	4,750
Goodwill	16,127
Current liabilities :	
Accounts payable and accruals :	
Trade	(819)
Others	(2,456)
Deferred income taxes	(2,207)
	24,614

e. Acquisition of Flavor Systems International Inc.:

On September 13, 2011, the Group signed through a US subsidiary an agreement to acquire 100% of the share capital of a US company – Flavor Systems International Inc. ("Flavor Systems"). The transaction was completed on October 3, 2011.

Flavor Systems in engaged in the development, production and marketing of sweet and savory flavors to the food and beverages markets. Flavor Systems owns a modern plant and R&D laboratories, located in Cincinnati, Ohio. The acquisition also includes a new and advanced production site. The site will enable expansion into market segments where the group is not active presently, such as the growing market for flavored coffee and shakes sold at convenience stores and large food chain stores in the US. In addition, through this acquisition, the group gains access for the first time to the US savory flavors market.

The operation of the acquired company was merged into the flavor activity of Frutarom in USA.

The final price of the transaction was determined in accordance with an agreed mechanism related to future considerations, based on a 6.5 multiplier of EBITDA exceeding $5 million gained by the operation of Flavor Systems during the 12 months starting on October 1, 2011 and ending on September 30, 2012 ("the target EBITDA"), up to a ceiling of $10 million. In addition, in the event that the target EBITDA during that period is less than $5 million, the sellers will repay up to $6 million to Frutarom. Therefore, the consideration for the acquisition may range from $28.8 million to $45.3 million, according to this mechanism. In addition, the Company paid $6.5 million for real-estate assets that are under the ownership of other companies owned by the shareholders of Flavor Systems.

NOTE 5 – BUSINESS COMBINATIONS (continued):

In accordance with the above-mentioned mechanism, the Group paid an additional amount of $ 10 million.

The cost of acquisition amounts to $ 35,262 thousands, with the addition of $ 10,000 thousands in accordance with the adjustment mechanism set in the acquisition agreement; the two amounts total $45,055 thousands. The acquisition was financed using long-term bank credit.

The cost of acquisition was allocated to acquired tangible assets, intangible assets and liabilities at their fair value on the date of acquisition.

Assets and liabilities of Flavor Systems at the date of acquisition:

	Fair value
	U.S. dollars in thousands
Current assets:	
Cash and cash equivalents	4
Accounts receivable:	
Trade	1,378
Inventory	2,120
Others	153
Non-current assets:	
Property, plant and equipment	10,871
Intangible assets:	
Goodwill	29,077
Product formulas	6,886
Customer relations	7,247
Current liabilities :	
Accounts payable	(1,101)
Short term bank credit	(195)
Others creditors	(729)
Deferred income taxes	(288)
Long-term loans	(10,368)
	45,055

f. 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.

NOTE 5 – BUSINESS COMBINATIONS (continued):

In the 12 months ended December 31, 2011, Savoury Flavours' sales turnover total amounted $7.1 million.

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):

g. 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

h. 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 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

i. 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. JannDeRee’s activities are synergetic with Frutarom’s activities in the field of flavors South Africa.

NOTE 5 – BUSINESS COMBINATIONS (continued):

In the twelve months ended December 31, 2012, JannDeRee's turnover amounted to approximately USD 5 million.

In the course of the third quarter 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):

j. 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. It is the Company's estimate that the acquisition of PTI will 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.

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.

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

As from the date it was consolidated with the financial statements of the Company through December 31, 2013, the acquired operations have yielded revenues of $ 35,396 thousands and net income of $ 1,527 thousands (net of acquisition costs and financing costs relating to the acquisition).

k. 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):

As from the date it was consolidated with the financial statements of the Company through December 31, 2013, the acquired operations have yielded revenues of $ 468 thousands and net loss of $ 26 thousands (net of acquisition costs in the amount of $ 115 thousands, net after tax).

l. 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 $ 40,074 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 assessment is performed for the Company and has not yet been completed as of the date of approval of these financial statements.

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	40,074
Current liabilities:	
Trade payables	(929)
Other payables	(1,168)
Deferred income taxes	(5,970)
	52,400

The results of Hagelin shall be consolidated as of December 31, 2013. Therefore the results of this company have not effect on income and loss for the year 2013.

m. Had the acquisitions been completed on January 1, 2013, 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, 2013 would have been $784,396 thousand, and net income for that year would have been $70,418 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.

Segment data provided to the chief operating decision-maker in respect of the reported segments for the year ended:

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):

31 December, 2011 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	369,894	142,176	6,373	-	518,443
Intersegment	-	2,832	-	(2,832)	-
Total sales and other operating income	369,894	145,008	6,373	(2,832)	518,443
Segment results	46,811	11,745	353	(245)	58,664
Financial expenses – net					5,798
Taxes on income					10,835
Net income					42,031

b. Additional information:

1) Geographical Segment information

The Group has operating production facilities in Europe, North America, Israel and Asia. In addition, the Group has 38 research and development laboratories and sells and markets its products principally through its 69 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		
	2013	2012	2011
	U.S. dollars in thousands		
EMEA*	471,499	428,174	359,238
America**	93,112	90,774	60,257
Asia and the Far East	66,492	57,982	55,053
Israel	42,590	41,071	43,895
	673,693	618,001	518,443

* Europe, Africa and the middle east (excluding Israel).

Sales in Germany amounted to $ 71,943 thousands, $ 74,085 thousands and $ 84,219 thousands in 2013, 2012 and 2011, respectively.

** In this report America includes sales in the USA amounting to $ 66,799 thousands, $ 63,906 thousands and $ 45,191 thousands in the years 2013, 2012 and 2011, respectively.

NOTE 7 – PROPERTY, PLANT AND EQUIPMENT

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 2012
	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

NOTE 7 – PROPERTY, PLANT AND EQUIPMENT (continued):

Composition of assets, grouped by major classifications and changes therein in 2012 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 2012
	U.S. dollars in thousands					U.S. dollars in thousands					
Land and buildings	84,991	2,951	(3)	64,804	152,743	14,277	3,607	-	25,999	43,883	108,860
Machinery and equipment	132,938	7,330	(538)	37,357	177,087	84,964	8,727	(315)	30,770	124,146	52,941
Vehicles and lifting Equipment	4,969	973	(545)	1,208	6,605	3,156	822	(450)	688	4,216	2,389
Furniture and office equipment (including computers)	35,626	979	(776)	4,867	40,696	16,900	1,571	(764)	3,834	21,541	19,155
Leasehold improvements	12,795	325	(12)	281	13,389	6,567	903	(8)	448	7,910	5,479
	271,319	12,558	(1,874)	108,517	390,520	125,864	15,630	(1,537)	61,739	201,696	188,824

* 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, 2013, in respect of the said lands, amount to$ 1,109 thousands (2012- $ 1,141 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 $ 167 thousand (2012 - $ 175 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 $ 1,812 thousands.

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 $ 3,336 thousands.

NOTE 8 – INTANGIBLE ASSETS:

	Original amount		Amortized balance	
	31 December		31 December	
	2013	2012	2013	2012
Know-how and product formulas	77,846	56,271	59,853	41,782
Goodwill	273,749	198,752	272,475	197,493
Customer relations	65,175	46,210	43,121	29,807
Trademarks	408	230	172	99
Computer software	26,839	25,264	8,108	10,017
	444,017	326,727	383,729	279,198

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 2012 – net	8,584	37,611	179,428	29,982	105	255,710
Changes in the year ended 31 December 2012:						
Acquisitions	2,284	-	-	-	-	2,284
Retirements during the year	(26)	-	-	-	-	(26)
Adjustment arising from acquisition of consolidated companies	1,752	6,921	15,733	3,702	-	28,108
Exchange differences	247	510	2,332	410	5	3,504
Annual amortization charge (Note 2f)	(2,824)	(3,260)	-	(4,287)	(11)	(10,382)
Closing net book amount	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

* Goodwill as of 31 December 2013 is allocated to the Flavor segment in the U.K., Germany, Israel, Norway, Italy, USA, Brazil, South Africa, Russia & Guatemala 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	
	2013	2012
	U.S. dollars in thousands	
Cash-generating unit 1	104,125	100,062
Cash-generating unit 2	36,120	36,120
Cash-generating unit 3	40,074	-
Cash-generating unit 4	20,536	-
Cash-generating unit 5	16,257	15,893
Cash-generating unit 6	11,306	11,053
Cash-generating unit 7	8,454	9,748
Cash-generating unit 8	7,008	6,705
Cash-generating unit 9	6,205	6,066
Cash-generating unit 10	6,901	-
Cash-generating unit 11	4,124	4,030
Cash-generating unit 12	3,549	-
Cash-generating unit 13	2,699	2,699
Cash-generating unit 14	2,619	2,619
Cash-generating unit 15	2,498	2,498
Total	272,475	197,493

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%-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 15% 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	
	2013	**2012**
	U.S. dollars in thousands	
Non current borrowings	140,113	137,836
Current borrowings:		
Current maturities of long-term loans	36,678	39,852
Bank borrowings	71,548	12,344
	108,226	52,196
Total borrowings	248,339	190,032

Bank borrowings as of December 31, 2013 mature until 2018 and bears average interest of 1.57% according to the loan terms and Libor rates as of 31 December, 2013
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**	
		2013	**2012**
		U.S. dollars in thousands	
Pound sterling	2.10%	13,853	22,694
Dollars	1.46%	151,679	53,552
Euro	1.95%	34,705	60,256
Swiss Franc	1.21%	46,127	46,177
NIS	-	-	5,893
Other currencies	7.60%	1,975	1,460
		248,339	190,032

* Interest rates as of 31 December, 2013

The long term liabilities (net of current maturities) mature in the following years after the balance
sheet dates:

	2013	**2012**
	U.S. dollars in thousands	
Second year	62,047	33,736
Third year	74,735	68,987
Fourth year	3,331	35,113
	140,113	137,836

The Group has several loans, in respect of which it has undertaken to meet certain financial covenants (see note 14). As of 31 December 2013, 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 2013, 2012 and 2011 are $ 2,622 thousands, $ 986 thousands and $ 2,144 thousands, respectively.

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, 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

	Present value of obligation	**Fair value of plan assets**	**Net liability (asset)**
	US dollars in thousands		
Balance as of January 1, 2012*	48,618	(32,480)	16,138
Current service cost	1,494	-	1,494
Interest expenses (income)	1,379	(896)	483
other	(991)	-	(991)
	1,882	(896)	986
Remeasurements of the net liability (asset):			
Return on plan assets, excluding amounts included in interest expense (income)	-	1,177	1,177
Loss (gain) from change in demographic assumptions	-	-	-
Loss (gain) from change in financial assumptions	5,291	-	5,291
Experience loss (gain)	(343)	-	(343)
	4,948	1,177	6,125
Differences from translation of financial statements	1,333	(809)	524
Employer's contributions	1,023	(2,430)	(1,407)
Benefit payments	(2,304)	2,123	(181)
Adjustment arising from acquisition of consolidated companies	2,144	-	2,144
	57,644	(33,315)	24,329

*Restated, see note 2x.

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	
	2013	*2012
	U.S. dollars in thousands	
Present value of obligations arising from fully or partially funded plans	56,872	57,644
Fair value of plan assets	(33,746)	(33,315)
Balance of liability recognized in the statement of financial position	23,126	24,329

*Restated, see note 2x.

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		
	2013	2012	2011	2013	2012	2011	2013	2012	2011
Discount rates	3.55%	4.15%	5.15%	3.36%	3.03%	4.77%	2.0%	1.8%	2.3%
Projected rates of payroll raise				1.17%	1.16%	1.16%	2.0%	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, 2013
	US dollars in thousands
Discount rate:	
1% increase	(8,333)
1% decrease	10,795
Salary growth rate:	
1% increase	1,123
1% decrease	(1,011)

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:

	2013	2012
	US dollars in thousands	
Government bonds	2,547	2,441
Real estate held abroad	3,421	3,293
Qualifying insurance policies	1,004	1,020
Cash and cash equivalents	23,794	23,411
other	2,980	3,150
Total	33,746	33,315

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 2014 and 2019.

Minimum lease commitments of the Group under the above leases, at rates in effect on 31 December 2013, are as follows:

	$ in thousands
Year ending 31 December:	
2014	6,007
2015	3,336
2016	2,525
2017	2,117
2018	1,104
2019	1,069
	16,158

Rental expenses totaled $ 6,518 thousand, $ 5,818 thousand and $ 4,673 thousand, in the years ended 31 December 2013, 2012 and 2011, 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 2013 is $1,230 thousand.
In 2013, 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 $31 thousand (2012 - $52 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	
	2013	2012
Authorized	100,000	100,000
Issued and paid	58,509	58,266

Company listed shares are quoted on the TASE at NIS 73.0 ($21.03) per share as of 31 December, 2013. 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 0.6% (323,183 shares) and 0.8% (477,711 shares) of the balance of ordinary issued and paid shares of this type as of 31 December 2013 and 2012, 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.
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 2013-01-111684)).

Through 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. 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.

The theoretical economic value of the options in respect of grants from 2007 through 2013, 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%-43.24%; risk-free interest rate of 2.2%-5.06% (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.

NOTE 12 – EQUITY (continued):

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, 2013:

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 $
2008	301	-	3.03
2009	1,912	-	2.85 – 2.98
2010	14,011	-	3.39 – 3.47
2011	4,569	18,318	3.49
2012	66,312	111,711	3.18 – 3.49
2013	-	100,667	4.78 – 5.79
	87,105	230,696	

As of 31 December, 2013, 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 $884 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.

The changes in the number of options outstanding and their related weighted average exercise prices are as follows:

	2013		2012		2011	
	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	3.10	462,036	2.97	417,342	3.10	424,098
Granted	5.25	103,192	3.15	228,914	3.59	73,348
Forfeited	3.26	(37,778)	3.08	(32,111)	3.07	(17,481)
Exercised	2.98	(209,649)	2.78	(152,109)	2.88	(62,623)
Balance at 31 December	3.99	317,801	3.10	462,036	2.97	417,342

NOTE 12 – EQUITY (continued):

The following table summarizes information about exercise price and the contractual terms of options outstanding at 31 December, 2013:

Share rights outstanding			Share rights exercisable		
Exercise Prices	**Number outstanding at December 31, 2013**	**Weighted average remaining contractual life**	**Weighted average exercise price**	**Number exercisable at December 31, 2013**	**Weighted average remaining contractual life**
$		Years	$		Years
2.82	301	0.75	2.82	301	0.75
2.65	253	1.25	2.65	253	1.25
2.77	1,659	1.75	2.77	1,659	1.75
3.22	3,156	2.25	3.22	3,156	2.25
3.15	10,855	2.75	3.15	10,855	2.75
3.24	22,887	3.25	3.24	4,569	3.25
2.96	43,589	3.75	2.96	26,068	3.75
3.25	56,175	4.25	3.25	15,717	4.25
3.21	78,259	4.75	3.21	24,527	4.75
4.78	52,778	5.25	4.78	-	5.25
5.79	47,889	5.75	5.79	-	5.75
	317,801			87,105	

3) In January 2006, the Company allotted 725,000 options, which are exercisable into 725,000 Company shares to four senior employees as part of a private offering; 350,000 of the said options were granted to the president of the Company and 125,000 were granted to a senior office holder. The options that were granted were exercisable in three equal batches which vested on 1.1.2008, 1.1.2009 and 1.1.2010. The exercise price is NIS 31.068 per share. The original expiry date of the options was 1 February, 2012. On 30 January 2012, the Company's Board of Directors resolved to extend the period till expiry by 1 further year till 31 January, 2013 ("extension period"). This resolution was made after the Company's Audit Committee approved the extension of the exercise period. All options were exercised in the course of the extension period.

The theoretical economic value of the allotted shares – computed using the Black & Scholes shares valuation model, amounted at date of grant to U.S. $1,620 thousand. This value is based on the following assumptions: expected dividend at a rate set to 0% in all years; standard deviation of expected share price returns of 29%-31%, annual risk-free interest at a rate of 4.35%-4.45% and an expected average option life until exercise of one year, two years, three years and four years.

The volatility measured at the standard deviation of expected share price returns is based on statistical analysis of weekly share price over the last twelve months, twenty four months and thirty six and forty eight months (in accordance with the vesting periods of the batches).

NOTE 12 – EQUITY (continued):

4) 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. 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.

In 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).

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 fair value of the options at date of grant - computed based on the binomial model – is NIS 4.7 million ($ 1.2 million); this value is based on the following assumptions: adjusted standard deviation of 29% per year, risk-free interest rate of 2.7% and termination rate (prior to end of the vesting period) of 11.5%; 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. 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 $ 30 thousand, $ 27 thousands and $30 thousand in 2013, 2012, 2011, respectively.

NOTE 12 – EQUITY (continued):

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 18, 2014, the Company's Board of Directors resolved to distribute a final cash dividend out of retained earnings as of December 31, 2013; the amount of this dividend is $4,732 thousand (NIS 16,382 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 2013 and 2012 amounted to $ 3,892 thousand (NIS 0.24 per share) and $ 3,029 thousands (NIS 0.2 per share). As mentioned in 2) above, the dividend in respect of the year ended 31 December 2013 at NIS 0.28 per share and totaling $4,732 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%.

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.

NOTE 13 - TAXES ON INCOME:

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 28%.
Companies incorporated in the UK – tax rate of 23% (April 2012 through March 2013 tax rate of 24%; 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 the Switzerland – tax rate of 22%.
Company incorporated in South Africa – tax rate of 28%
Companies incorporated in Russia – tax rate of 20%
Companies incorporated in Guatemala – tax rate of 31%

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.
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.

NOTE 13 –TAXES ON INCOME (continued):

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%.

As a result of an amendment of tax rates in 2013, deferred tax liability increased in the amount of $385 thousand.

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:

		Provisions for employee rights						
	Depreciable fixed assets	Severance Pay	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, 2012	12,961	*(2,265)	(175)	(929)	(126)	12,347	(427)	21,386
Changes in 2012:								
Additional taxes as a result of acquisition of Subsidiaries	3,095	-	-	(27)	(17)	2,266	(3,329)	1,988
Differences from translation of foreign currency financial statements of subsidiaries	313	(27)	-	33	22	393	(112)	622
Charged directly to the equity	-	(1,661)	-	-	-	-	-	(1,661)
Amounts carried to income statement	226	(77)	(15)	(290)	(484)	1,461	(1,811)	(990)
Balance at 31 December 2012	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

*Restated

NOTE 13 –TAXES ON INCOME (continued):

2) Deferred taxes are presented in the statements of financial position as follows:

	December 31	
	2013	2012
	U.S. dollars in thousands	
Among non-current assets	3,424	3,075
Among non-current liabilities	(34,084)	(24,420)
	(30,660)	(21,345)

3) The deferred taxes in respect of Group activities in Israel are computed at the tax rate of 16% (2012 – 13%). 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:

	2013	2012	2011
	U.S. dollars in thousands		
Current taxes:			
For the reported year's income	19,056	15,335	11,592
Adjustments in respect of previous years	(642)	(717)	(1,114)
	18,414	14,618	10,478
Deferred taxes:			
Creation and reversal of deferred taxes	(2,806)	(990)	357
T o t a l	15,608	13,628	10,835

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:

	2013	2012	2011
	U.S. dollars in thousands		
Income before taxes on income, as reported in the income statements	79,229	65,608	52,866
Theoretical tax expense in respect of this income – at 25% (2012 – 25%; 2011 – 24%)	19,807	16,402	12,688
Less – tax benefit arising from approved enterprise /benefited enterprise status	(2,097)	(1,158)	(1,788)
Increase in taxes resulting from different tax rates applicable to foreign subsidiaries	(391)	52	1,167
Decrease in taxes arising from computation of deferred taxes at a rate which is different from the theoretical rate	(209)	(159)	331
Increase (decrease) in deferred taxes as a result of future changes in the tax rates	(2,089)	-	(170)
Increase (decrease) in taxes arising from permanent differences – disallowable expenses (income)	501	(412)	(76)
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)	(482)	(372)	(151)
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	(74)	(8)	(52)
Taxes on income for the reported year	14,966	14,345	11,949

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.
On January 1, 2013, the Income Tax Authority issued a notice regarding the extension of the term of the temporary order to tax year 2012 (hereafter – "the Tax Authority's notice"). In its notice, the Tax Authority states that it intends to promote legislation to extend the term of the said temporary order by one additional year to 2012 as soon as the Knesset reconvenes. Nevertheless, in practice the no legislative measures came into effect that extend the terms of the temporary order.
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 2011 shall be extended to 2012 -2013 as well. In view of the fact that the temporary order applies to tax years 2007 to 2011 as above and in view of the potential extension of the term of the temporary order to 2012-2013, the Group's management expects that at this stage the new legislation shall not apply to tax years preceding 2014.

Taking into consideration the temporary order which applies to tax years 2007 to 2011 and the Company's estimate regarding the potential extension of the term of the temporary order to 2012 and 2013 as above, the Company computed its taxable. The amendment to the ordinance did not have a material effect on the tax expenses reported in these financial statement.

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 31.12.2013 the Group's equity amounts to $ 521,059 thousands.
   2) The amount representing the Group's equity would not be lower than 35% of total assets. As of 31 December, 2013, the Company's equity equals 53.7% 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, 2013 the said ratio is 1.6.

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 2013, the ratio was 0.69.

   2) The amount of equity shall not be lower than 35% of total balance sheet of the Swiss group. As of 31 December 2013 the ratio was 42.5%.

As mentioned above, as of 31 December 2013, the Group meets its obligations.

NOTE 15 – ACCOUNTS RECEIVABLE:

	December 31	
	2013	2012
	U.S. dollars in thousands	
a. Trade – composed as follows:		
Open accounts	136,065	104,396
Interested parties	-	342
	136,065	104,738
Cheques collectible	2,308	2,016
	138,373	106,754
The item includes – provision for doubtful accounts	6,076	3,640

As of 31 December, 2013 certain trade receivable balances– amounting to $ 26,870 thousands (2012 - $ 22,636 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 $1,318 thousand (2012 - $ 961 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	
	2013	2012
	U.S. dollars in thousands	
Through 90 days	25,414	21,694
90 to 120 days	1,456	942
	26,870	22,636
Provision for doubtful accounts	(1,318)	(961)
	25,552	21,675

As of 31 December, 2013, the Company made a provision for doubtful accounts in respect of balances in the total amount of $5,126 thousand (2012 – $2,957 thousand) in arrears of more than 120 days. The amount of the provision as of 31 December, 2013 was $4,750 thousand (2012 – $2,379 thousand).

NOTE 15 – ACCOUNTS RECEIVABLE (continued):

The aging of the said balances is presented below:

	December 31	
	2013	2012
	U.S. dollars in thousands	
120 days to 1 year	1,117	1,483
Over 1 year	4,009	1,474
	5,126	2,957
Provision for impairment of receivables	(4,750)	(2,379)
	376	578

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	
	2013	2012
	U.S. dollars in thousands	
b. Other:		
Employees and institutions	346	398
Government institutions	8,122	9,173
Sundry	3,974	1,378
	12,442	10,949

NOTE 16 – INVENTORIES

	December 31	
	2013	2012
	U.S. dollars in thousands	
Raw materials and supplies	71,989	61,180
Products in process	11,453	10,697
Finished products	60,029	48,299
	143,471	120,176
Inventories for commercial operations – purchased products	11,250	2,257
	154,721	122,433

NOTE 17 – OTHER

	December 31	
	2012	2013
	U.S. dollars in thousands	
Prepaid expenses in respect of operating lease	47	60
Sundry	68	217
	115	277

NOTE 18 – CASH AND CASH EQUIVALENTS:

Classified by currency, linkage terms, the cash and cash equivalents are as follows:

	December 31	
	2013	2012
	U.S. dollars in thousands	
In Dollars	13,220	18,157
In Pounds sterling	4,627	2,953
In Euro	22,248	19,046
In Swiss Francs	3,297	3,533
Yuan	4,388	2,878
NIS	467	1,008
Brazilian real	2,403	3,257
Ruble	3,537	-
Other	3,425	3,101
	57,612	53,933

NOTE 19 – ACCOUNTS PAYABLE:

	December 31	
	2013	2012
	U.S. dollars in thousands	
a. Trade:		
Open accounts	58,407	48,237
b. Other:		
Payroll and related expenses	13,052	11,439
Government institutions	17,704	14,682
Provision for commissions and discounts	3,516	2,527
Accrued expenses	14,719	8,674
Provisions	166	320
Conditional consideration in respect of acquisition of subsidiaries	1,980	657
Sundry	1,626	970
	52,763	39,269

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		
	2013	2012	2011
	U.S. dollars in thousands		
a. Cost of Sales:			
Industrial operations:			
Materials consumed	288,410	279,694	256,031
Payroll and related expenses	53,410	48,763	44,408
Depreciation and amortization	13,327	13,134	11,209
Other production expenses	35,901	32,734	29,206
	391,048	374,325	340,854
Decrease (increase) in work in process and finished products inventories	(6,817)	(1,876)	(16,034)
	384,231	372,449	324,820
Commercial operations – cost of products sold	32,666	19,293	5,046
	416,897	391,742	329,866
b. Selling, Marketing, Research and Development Expenses – net:			
Payroll and related expenses	59,017	54,369	48,136
Transportation and shipping	17,138	16,196	14,335
Marketing commissions	6,471	5,841	3,742
Doubtful accounts	982	(441)	(347)
Depreciation and amortization	9,230	8,510	5,984
Travel and entertainment	4,240	4,015	3,416
Office rent and maintenance	4,641	4,818	3,902
Other	13,504	11,624	9,473
	115,223	104,932	88,641
The item includes expenses for product development and research activities, net*	29,829	28,031	24,333
* net of participation from government departments and others	182	384	655

	Year ended 31 December		
	2013	2012	2011
	U.S. dollars in thousands		
c. General and Administrative Expenses:			
Payroll and related expenses	30,476	28,852	23,864
Depreciation and amortization	4,442	4,368	3,419
Professional fees	3,860	3,094	2,110
Communication, office supplies and Maintenance	5,319	5,266	4,416
Travel and entertainment	1,927	1,595	1,686
Other	6,107	6,022	3,736
	52,131	49,197	39,231

NOTE 20 – INCOME STATEMENT ANALYSIS (continued):

	Year ended 31 December		
	2013	**2012**	**2011**
	U.S. dollars in thousands		
d. Other Expenses (income) – net:			
Capital loss on sale of fixed assets	(150)	92	17
Expenses relating to acquisition of subsidiaries	918	954	1,876
Expenses for institutional audit	-	-	150
Expenses for site shutdown*	2,095	-	-
Other	(178)	(35)	(2)
Income from bargain purchase	-	(1,729)	-
	2,685	(718)	2,041

* As part of the procedures designed to increase the efficiency of its operations, the Company completed during the reported period the transfer of production operations conducted in the Nesse site located in Germany to other Company sites. In the reported period, the Company recorded in respect of the above one-off expenses relating to re-organization and fixed assets depreciation.

e. Financial Expenses – net:			
In respect of long-term loans and credit	2,498	5,154	1,489
In respect of exchange differences of trade receivables and trade payable balances – net	1,908	48	3,254
In respect of cash and cash equivalents, short-term deposits and loans, short-term credit and other – net	3,122	2,038	1,055
	7,528	7,240	5,798

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.

	2013	2012	2011
Income (expenses):	U.S. dollars in thousands		
Sales – affiliates (companies controlled by the controlling shareholder):			
Fallek Chemical Japan	206	574	405
Other	8	4	9
	214	578	414
Purchases:			
Affiliates (companies controlled by the controlling shareholder):			
Azur S.A	(1,744)	(1,743)	(1,819)
Dividend	(1,439)	(1,132)	(1,257)
Other expenses:			
Affiliates -			
Azur S.A.	(21)	(42)	(35)
Benefits to related parties:			
Wages and salaries	(2,810)	(2,603)	(2,119)
Director fees (in the Company)	(209)	(186)	(192)

2) Shares granted to the President of the Company

As part of the Board resolution, the President of the Company was granted, on 2 January 2006, 350 thousand options; the fair value of options that the Company allotted to the President, computed using the Black & Scholes shares valuation model (based on the assumptions described in Note 12c), was estimated at the date of grant to $783 thousand (Note 12c).

On January 30, 2012, the Company's board of directors resolved to extend by one year the exercise period of the options until 31 of January 2013. The total benefit granted to the President due to the extension is $202 thousand.

On July 15, 2010, 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 $ 322 thousands at date of grant.

NOTE 21 – RELATED PARTIES – TRANSACTIONS AND BALANCES (continued):

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.

The total benefit component granted to the President (see note 12) in the years 2013, 2012 and 2011 as computed at date of grant is $230 thousand, $806 thousand and $156 thousand, respectively.
Benefit costs that have been charged to the income statements, in respect of the said shares granted in the years 2013, 2012 and 2011 are $423 thousand $ 513 thousands and $216 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:

3.1 Basic monthly salary – up to NIS 220 thousands.

3.2 Social benefits ancillary benefits: as specified in the compensation policy, including severance pay of up to 200% of the severance pay by law and 13th salary.

3.3 Terms of termination of employment: advance notice of 6 months and increased severance pay as specified above. Also, in the event the president's employment is terminated during a period of up to 12 months from the time at which ICC Handels AG's holdings in the Company have fallen below 26%, the president will be entitled to his Basic Wage (not including vacation, sickness, bonuses and options) for a period of up to 12 months starting from the end of the advance notice period prescribed for president. In addition, in such event the president of the Company shall be allowed to immediately exercise of all options granted to him in the past, even if the vesting period has not been completed.

3.4 Annual bonus – paid in cash and in equity:

Threshold conditions: Bonuses for office holders are contingent on office holder’s fulfillment of cumulative threshold conditions, to be calculated on the basis of the Company’s reports as follows:

- Consolidated EBITDA, after deduction of one-off events, higher than US$80 million.

NOTE 21 – RELATED PARTIES – TRANSACTIONS AND BALANCES (continued):

- Consolidated net profit, after deduction of one-off events, net of bonuses, higher than US$25 million.

Some of the bonus to the Company's president shall be paid in cash and the remaining amount shall be paid as a deferred equity bonus determined as follows:

EBITDA	**Annual Bonus**		
Less one-off events	**In cash**	**Deferred equity**	**Total**
145,000	1,620	380	2,000
140,000	1,580	345	1,925
135,000	1,560	335	1,895
130,000	1,540	325	1,865
125,000	1,470	315	1,785
120,000	1,400	305	1,705
115,000	1,330	295	1,625
110,000	1,260	285	1,545
105,000	1,190	270	1,460
100,000	1,120	250	1,370
95,000	1,050	220	1,270
90,000	980	185	1,165
85,000	880	150	1,030
80,000	780	110	890

The cash bonus shall be paid as part of the first salary paid after the approval of the annual financial statements of the Company.

The equity bonus will be paid in options for the purchase of Company shares, whose total market value at the time of purchase will be equal to 1.5 times the rate of the aforesaid bonus component, to the effect that the rate of the bonus will constitute a benefit of 2/3 of the value of the options granted to president of the Company, and the exercise price of the options to be paid to the president of the Company shall constitute 1/3 of the value of Company's shares as of the date of purchase thereof (for details regarding the conditions for exercise of the options see Note 12 and the compensation policy).

The ceiling for the annual bonus, including the cash component and the equity based component as described above shall not exceed $ 2 million.

3.5 Equity based bonus:

The Company reserves the right to grant senior office holders options for ordinary shares in accordance with the equity based bonus plan adopted from time to time, subject to the provisions of law.

3.6 One-off bonus: The Board of Directors may resolve to grant a one-off bonus during the course of the policy period, for recognized achievement on the part of an office holder, as part of a transaction not in the ordinary course of business for the Company (hereinafter "one-off bonus").

NOTE 21 – RELATED PARTIES – TRANSACTIONS AND BALANCES (continued):

One-off bonuses shall not exceed three salaries. Should a one-off bonus be paid, it shall be separate and unrelated to the annual bonus. A one-off bonus shall only paid once in the course of the policy period.

In accordance with the compensation policy, the possible ratio range between the components of the overall compensation to the Company's president for a given year and the fixed compensation components in annual terms is: minimal fixed compensation cost – 25% and maximum variable compensation cost – 75% (excluding one-off bonus).

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.

b. Balances with Related Parties:

	31 December		
	2013	**2012**	**2011**
	U.S. dollars in thousands		
1) Current receivables – presented among “other receivables-other” and “trade receivables"			
Affiliated companies:			
Fallek	-	342	137
ICC	2	-	2
	2	342	139
Highest balance during the year	342	342	221
2) Current payables shareholder and related parties:			
Azur S.A.	228	18	57
	228	18	57

NOTE 22 – SUBSEQUENT EVENTS:

a. **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, intellectual property 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$7.5 million and also includes additional future payment based upon CitraSource's performance over 2014-2018.

The acquisition was funded using bank credit.

NOTE 22 – SUBSEQUENT EVENTS (continued):

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 a worldwide sourcing network in citrus

CitraSource's activity will be integrated into Frutarom's flavor and fragrance activity.

b. **Distribution of dividend**

On March 18, 2014 the Company’s Board of Directors declared the distribution of a dividend of NIS 0.28 per share. Total amount of the dividend is $4,732 thousand (based on exchange rate as of date of confirmation of these financial statements).

NOTE 23 – LIST OF CONSOLIDATED SUBSIDIARIES AND INVESMENT IN SUBSIDIARIES

a) LIST OF CONSOLIDATED SUBSIDIARIES

Name of company	Country	Percentage of shareholding and control 31 December 2013 %	2012 %
Subsidiaries:			
Frutarom Ltd.(1)	Israel	100	100
Frutarom Trust Ltd.(2)	Israel	-	100
(1)Frutarom Ltd. holds the following companies:			
Frutarom Trade and Marketing (1990) Ltd.	Israel	100	100
Galilee Essences Ltd.(3)	Israel	-	-
Frutarom (UK) Holdings. (4)	U.K.	100	100
International Frutarom Corporation (5)	U.S.A	100	100
Frutarom Russia Ltd.	Russia	100	100
Frutarom Ukraine Ltd.	Ukraine	100	100
Frutarom Kazakhstan LLp.	Kazakhstan	100	100
Frutarom Flavors (Kunshan) Company (21)	China	100	100
Frutarom Gida Urunleri San. ve Tic.Ltd. Sti.	Turkey	100	100
Frutarom Mexico S.A	Mexico	100	100
Frutarom do Brazil Ltd.(6)	Brazil	100	100
Frutarom F&F (Shanghai) Trading .co.Ltd.	China	100	100
Frutarom South Africa (Proprietary) Ltd.	South Africa	75	75
Turkish Holdings Ltd. (3)	Turkey	100	100
Notra Liz Ltd.	Israel	55	55
Frutarom (Asia Pacific) Ltd.(7)	Hong Kong	100	100
Frutarom Singapore Pte Ltd.	Singapore	100	100
Frutarom Flavours (India) Private Limited	India	100	-
Frutarom Flavors and Ingredients (Shanghai)	China	100	100
Frutarom Nigeria Ltd.	Nigeria	100	-

(2)The company has been closed in 2012.
(3)Inactive company

(4) Frutarom (UK) Holdings Ltd. holds full ownership in the following companies:			
Frutarom Switzerland Ltd.(8)		100	100
Frutarom (UK) Ltd.(9)		100	100
Frutarom Italy S.R.L. (10)		100	100
Frutarom Norway A.S.		100	100
Frutarom - Etol (UK) Limited (22)		100	-
(5) International Frutarom Corporation holds the following companies:			
Frutarom U.S.A. Inc.(11)		100	100
Frutarom Flavor & Fragrance Costa Rica SRL.		100	100
(6) Frutarom do Brazil Ltd holds full ownership in:			
Vila Osorio Participacoes S/A(12)		100	100
(7) Frutarom (Asia Pacific) Ltd. holds in the following companies:			
Frutarom Flavors & Ingredients (Shanghai) (**)		99	99

NOTE 23 – LIST OF CONSOLIDATED SUBSIDIARIES (continued):

Name of company	Country	Percentage of shareholding and control 31 December 2013 %	2012 %
(8) Frutarom Switzerland Ltd. has full ownership in the following companies:			
Frutarom Germany GmbH(13)		100	100
Frutarom Nordic A/S		100	100
Frutarom France S.A.R.L		100	100
Frutrarom (Marketing) S.R.L(3)		100	100
Frutarom Netherlands B.V.(14)		100	100
Frutarom Etol Tovarna arom in etericnih d.o.o(15).		100	100
International Aroma Group (23)		100	-
Vantodio Holdings Limited (24)		75	-
(9) Frutarom (UK) Ltd. has full ownership in the following companies:			
Aromco Ltd.(16)		100	100
Savoury Flavors (Holdings) Ltd (17)		100	100
(10) Frutarom Italy S.R.L. has holdings in the following companies:			
Frutarom Czech Republic S.r.o. (***)		90	90
(11) Frutarom U.S.A. Inc. has full ownership in the following companies:			
Frutarom USA Holdings Inc.		100	100
Flavors system International Inc.(18) (2)		-	100
Hagelin & Company LLC.		100	-
(12) Vila Osorio Participacoes S/A has holdings in the following companies:			
Mylner Industria E Comercio Ltda		100	100
(13)Frutarom Germany GmbH has holdings in the following companies:			
Frutarom Savory Solutions GmbH (19)		100	100
(14)Frutarom Netherlands B.V. holds full ownership in the following companies:			
Frutarom Belgium N.V.		100	100
(15) Frutarom Etol Tovarna arom in etericnih olj d.o.o has holdings in the following companies:			
Frutarom Polska SP z.o.o.		100	100
Etol JVE d.o.o.		100	100
Etol Skopje (20)		100	100
Etol Kazahstan t.o.o.		100	100
Etol SK s.r.o. CZ		100	100
Etol Russia Ltd.		100	100
Etol Proizvodnja Arom D.O.O		100	-

NOTE 23 – LIST OF CONSOLIDATED SUBSIDIARIES (continued):

Name of company	Country	Percentage of shareholding and control 31 December 2013	2012
		%	%
(16) Aromco Ltd. has holdings in the following companies::			
Aromco South Africa (PTY) Ltd		100	100
MIS Aromco Flavors India (p) Ltd		100	100
(17) Savoury Flavors (Holdongs) Ltd has holdings in the following companies::			
Savoury Flavors Ltd.		100	100
Imarco Food Ingredients Ltd.		100	100
(18) Flavors system International Inc. holdings in the following companies::			
FSI Beverage System, LLC (2)		-	100
FSI Fragrance, LLC (2)		-	100
(19) Frutarom Savory Solutions GmbH holdings in the following companies::			
GewürzMüller AG(3)		100	100
NESSEpol Sp. z.o.o (merge to Frutarom Polska SP z.o.o.)		-	100
(20) Etol Skopje holdings in the following companies::			
Ingrediants dooel Skopje		100	100
(21) Frutarom Flavors (Kunshan) Company holdings in the following companies:			
Pucheng Yongfang Fragrance		51	51
(22) Frutarom - Etol (UK) Limited holdings in the following companies:			
Frutarom - Etol Ukraine LLC.		100	-
(23) International Aroma Group holdings in the following companies: (directly or indirectly)			
Mark Service		100	-
Chemical Process		100	-
Hexachem S.A		100	-
Aroma S.A		100	-
(24) Vantodio Holdings Limited holdings in the following companies: (directly or indirectly)			
CASPIAN LTD BVI, Alpris LTD Cyprus			
Rosable LTD BVI, Gibl LTD Cyprus			
PTI Group of Companies LLC			
Tekhnomol Soya Products LLC			
Platinum Absolute LLC, PTI-centre LLC			
PTI-Nord LLC, PTI-Irkutsk LLC			
PTI-Ural LLC, PTI-South LLC			
PTI-Voronezh LLC, PTI-Vladivostok LLC			
Petrovskoe-7 LLC, PTI Astana LLC			
PTI-BEL PTUE, PTI-Ukraine LLC			
PTI-MOL LLC, PTI-Logistika LLC			

NOTE 23 – LIST OF CONSOLIDATED SUBSIDIARIES (continued):

(*) the remaining percentage is held by Frutarom Industries .Ltd.
(**) the remaining percentage is held by Frutarom F&F (Shanghai) Trading .co.Ltd.
(***) the remaining percentages are held by Frutarom (UK) Holdings.

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 2013	
			U.S. dollars in thousands	
Frutarom Ltd.	Israel	100%	402,169	113,004

CHAPTER D

ADDITIONAL INFORMATION

Chapter D – Additional Details

Table of Contents

Company name:	**Frutarom Industries Ltd.**
Company 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, 2013**
Date of report:	**March 18, 2013**
Period of report:	**January 1, 2013 - December 31, 2013**

Regulation 10A - Summary of Quarterly Profit and Loss Reports

The following is the summary of the total profit of the corporation for each of the calendar quarters in the reported year:

IN US$ 000	Q1 - 2013		Q2 -2013		Q3 - 2013		Q4 - 2013		2013 Total	
SALES	**152,165**	**100.0%**	**168,648**	**100.0%**	**161,046**	**100.0%**	**191,834**	**100.0%**	**673,693**	**100.0%**
Cost of sales										
Material consumed	70,974	46.6%	78,253	46.4%	74,786	46.4%	94,858	49.4%	318,871	47.3%
Other manufacturing	24,015	15.8%	23,545	14.0%	23,698	14.7%	26,768	14.0%	98,026	14.6%
Total	**94,989**	**62.4%**	**101,798**	**60.4%**	**98,484**	**61.2%**	**121,626**	**63.4%**	**416,897**	**61.9%**
GROSS PROFIT	**57,176**	**37.6%**	**66,850**	**39.6%**	**62,562**	**38.8%**	**70,208**	**36.6%**	**256,796**	**38.1%**
R&D, Selling and G&A										
R&D	7,092	4.7%	7,571	4.5%	7,566	4.7%	7,600	4.0%	29,829	4.4%
Selling expenses	18,415	12.1%	19,831	11.8%	19,857	12.3%	27,291	14.2%	85,394	12.7%
General & Administration	12,761	8.4%	12,524	7.4%	12,544	7.8%	14,302	7.5%	52,131	7.7%
Other expenses	3	0.0%	1,992	1.2%	25	0.0%	665	0.3%	2,685	0.4%
Total	**38,271**	**25.2%**	**41,918**	**24.9%**	**39,992**	**24.8%**	**49,858**	**26.0%**	**170,039**	**25.2%**
OPERATING PROFIT	**18,905**	**12.4%**	**24,932**	**14.8%**	**22,570**	**14.0%**	**20,350**	**11.0%**	**86,757**	**12.9%**
Financing expenses	1,258	0.8%	1,181	0.7%	1,185	0.7%	1,996	1.0%	5,620	0.8%
Translation (gain) losses	161	0.1%	1,110	0.7%	109	0.1%	528	0.3%	1,908	0.3%
Total	1,419	0.9%	2,291	1.4%	1,294	0.8%	2,524	1.3%	7,528	1.1%
PROFIT BEFORE TAX	**17,486**	**11.5%**	**22,641**	**13.4%**	**21,276**	**13.2%**	**17,826**	**9.3%**	**79,229**	**11.8%**
TAX	3,478	2.3%	5,009	3.0%	4,250	2.6%	2,871	1.5%	15,608	2.3%
Tax rate	19.9%		22.1%		20.0%		16.1%		19.7%	
NET PROFIT	**14,008**	**9.2%**	**17,632**	**10.5%**	**17,026**	**10.6%**	**14,955**	**7.8%**	**63,621**	**9.4%**

Regulation 10C - Use of Securities' Proceeds

Not relevant.

Regulation 11 – List of Investments in Subsidiaries and Related Companies

Name of company	Type of Share	Par Value	Number of Shares	Total Par Value	Holding %		
					Equity	Voting	Right to appoint director
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 rates of holding, see Note 23 to the Company's financial statements of December 31, 2013.

Regulation 12 - Changes in Investments in Subsidiaries and Related Companies

A. JannDeRee (Pty) Limited

On May 2, 2013 Frutarom, through a South African subsidiary, acquired 100% of the share capital of the South African flavors company JannDeRee (Pty.) Limited for a cash payment of USD 5 million.

For further details regarding the acquisition see the Company's immediate report dated May 2, 2013.

B. Protein Technologies Ingredients

On November 20, 2013 Frutarom, through a Swiss subsidiary, acquired 75% of the share capital of the Cypriot company Vantodio Holdings Limited ("Vantodio"), holder of the Russian Protein Technologies Ingredients group ("PTI") in consideration for US$50.3 million. The acquisition agreement includes a mutual option for the purchase of the remaining 25% of Vantodio's share capital by Frutarom.
For further details regarding the acquisition see the Company's immediate reports dated November 18 and 20, 2013.

C. International Aroma Group

On November 25, 3013 Frutarom, through a Swiss subsidiary, acquired 100% of the share capital of International Aroma Group, a Panama flavors company, holder of the Guatemalan Aroma group, in return for cash payment of US$12.5 million. The acquisition agreement contains a mechanism for future payment of additional consideration.

For further details regarding the acquisition see the Company's immediate report dated November 25, 2013.

D. Hagelin & Company Inc.

On December 11, 2013 Frutarom, through a US subsidiary, acquired 100% of the share capital of the US based Hagelin and the US based BRC Operating Company LLC , in return for a cash payment of US$52.4 million.

For further details regarding the acquisition see the Company's immediate report dated December 12, 2013.

E. CitraSource LLC – after the balance sheet date, on February 24, 2014, Frutarom, through aUS subsidiary, acquired the business and assets of the US based CitraSource LLC and all holdings in the Florida based CitraSource Holdings LLC for a consideration of US$7.5 million. The acquisition agreement also includes a mechanism for future payment of additional consideration.

For further details regarding the acquisition see the Company's immediate report dated February 25, 2014.

For more details regarding the subsidiaries in the Frutarom Group see Note 23 to the Company's financial statements of 31 December 2013.

Regulation 13 - Income of and from Subsidiaries and Related Companies

Company name	Profit (loss) for the reporting period (US$ 000)	Other profit (loss) (US$ 000)	Total profit (loss) for the reporting period	Dividend (US$ 000)		Management fee (US$ 000)		Interest	
				Before the reporting period	After the reporting period	Before the reporting period	After the reporting period	Before the reporting period	After the reporting period
Frutarom Ltd.	55,112	12,903	68,015	3,892	-	-	-	-	-

Regulation 14 – Loans

Granting loans is not one of the Group's main business activities.

Regulation 20 - Trade on the Stock Exchange

During the reporting period the Company issued 243,008 additional ordinary shares of NIS 1 par value each.

During the reporting period trade in the Company's shares was not halted.

Regulation 21 –Payments to Interested Parties and Senior Officeholders

Section (a) (1)

Following are details regarding the remuneration recorded in the Company's Financial Report for the period ended December 31, 2013 made to each of the five most highly remunerated senior officeholders in the Company or corporation under its control that was paid 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%	1.72% [7]	980	1,407	423 [8]	-	-	-	-	-	-	-	2,810
Amos Anatot	EVP – Supply Chain [9]	100%	0.24% [10]	299	144	122 [11]								565
Alon Granot	EVP & CFO [12]	100%	0.21% [13]	273	144	118 [14]	-	-	-	-	-	-	-	535
Guy Gill	VP – Finance [15]	100%	0.09% [16]	173	58	61 [17]	-	-	-	-	-	-	-	292
Tali Mirsky Lachman	Global VP – Legal & Company Secretary [18]	100%	0.13% [19]	143	58	70 [20]	-	-	-	-	-	-	-	271

Notes to the above table:
[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, telephone, social benefits, provisions for termination of employment and any other payment made to the senior officeholders).
[4] For details regarding the determination of bonuses by the Board of Directors and Compensation Committee, see section E in the section Corporate Governance in the Company's Board of Directors' Report for December 31, 2013. It should be noted that starting in 2014 all bonuses to senior officeholders will be granted in accordance with the Company's Compensation Policy (for further details regarding the Compensation Policy approved see the immediate report on the matter, published on December 29, 2013).
[5] Since 2003, the Company's Board of Directors has every six months resolved with regards to granting options to senior officeholders and other senior employees, based on the recommendations of the Compensation Committee. Based on the Board's resolution and taking into account the number of outstanding shares available to the Company for grant of options, the Company then buys its shares on the Tel Aviv Stock Exchange and as against these shares, options are granted. Until 2011, these options were granted under the 2003 Option Plan (**"2003 Plan"**). Starting from 2012, these options are granted under the 2012 Option Plan ("**2012 Plan**"). The options are vested over a three year period from the date on which they were granted, one third every year. The Board of Directors of the Company has the exclusive authority to declare the vesting of the options as of any earlier date. The Board of Directors has set the exercise price for the options at one third of the average share price paid by the Company for the shares. Options granted under these plans expire on the sixth anniversary of the grant date. Any tax consequences or liabilities arising from the grant or exercise of any options are the responsibility of the employee. The number of shares allocated per option granted under these plans and the exercise price are adjusted according to changes in the Company's outstanding share capital resulting from a stock split, reverse stock split, stock dividend, combination or reclassification of shares. Other than a few exceptions, in the event of termination of employment, the employee has the right to exercise all vested options within 90 days from the date of termination. Any remaining options granted but not exercised as above are forfeited. Options not vested on the date of the termination of employment are immediately forfeited on that date. Starting in 2013, the grant of options to Mr. Ori Yehudai under the 2012 Plan is under the equity component of the annual bonus (for further details regarding the employment agreement of the President and CEO of the Company, see the immediate report on the matter, published on June 27, 2013). Starting in 2014 and in accordance with the Company's Compensation Policy, approved on January 14, 2014, the granting of options under the 2012 Plan to all senior officeholders in the Company, including the President and CEO of the Company, is included in the deferred equity component of the annual bonus (for further details regarding the Compensation Policy approved see the immediate report on the matter, published on December 29, 2013).
In January 2006, the Company granted 725,000 options exercisable into 725,000 ordinary shares of the Company to four senior employees, 350,000 of which were

granted to Mr. Ori Yehudai and 125,000 of which were granted to Mr. Alon Granot. The options granted were exercisable in three equal portions which vested on January 1, 2008, January 1, 2009 and January 1, 2010. The exercise price was NIS 31.068 per share. The original expiry date of the options was on February 1, 2012, and on January 30, 2012 the Board of Directors, after the approval of the Audit Committee, resolved to extend the expiry date by one year, until January 31, 2013 (the **"Extension Period"**). Over the Extension Period, all the above options were exercised.

On July 15, 2010 the Company's Board of Directors approved an option plan for senior management ("**2010 Plan**"). The options granted under this plan are vested in three equal tranches, at the end of every year starting from the end of the second year following the grant. The Company's Board of Directors has exclusive authority to declare the vesting of the options at an earlier date. All tax liabilities deriving from the granting of options and/or their exercise devolve upon the employee. The number of shares allocated per option granted under these plans and the exercise price are adjusted according to changes in the Company's outstanding share capital resulting from a stock split, reverse stock split, stock dividend, combination or reclassification of shares. Other than a few exceptions, in the event of termination of employment the employee has the right to exercise all vested options within 90 days from the date of termination. Any remaining options granted but not exercised as above are forfeited. Options not vested on the date of the termination of employment are immediately forfeited on that date

At the time of approval of the 2010 Plan, the Company's Board of Directors, following the recommendation of the Compensation Committee, approved the grant of up to 1,000,000 options to Mr. Yehudai and 10 more employees and officeholders in the Group, as well as additional quantity of up to 255,000 options to be granted in the future to employees and officeholders in the Group (the **"Options for Future Allocation"**). Grant of these options to Mr. Yehudai was also approved by the Company's Audit Committee. The options were granted for no consideration. The exercise price of options under this grant was NIS 30.26, which is the closing price of the Company's share on the last trading day prior to the Board of Directors' resolution on the grant of the options. Furthermore, it was resolved that every Option for Future Allocation granted to the Company's future grantees under this grant will be exercisable into one share for an exercise price equal to the average of the Company shares' closing price over the last ten (10) trading days prior to the Board of Directors' resolution on the future grant, provided the exercise price for each Option for Future Allocation will not be less than the par value of the exercisable share.

On February 6, 2011 40,000 options were granted to a senior officeholder in the Company, as part of this grant (out of the Options for Future Allocation). This grant was also approved by the Audit Committee and by the Board of Directors, and the exercise price was set at NIS 36.93.

On August 20, 2012 the Company's Board of Directors, following the recommendation of the Compensation Committee, approved the grant of up to 945,000 options unregistered for trade, under the 2010 Plan, to Mr. Yehudai and to another 10 employees and officeholders in the Group, and an additional 200,000 Options to be allocated in the future to employees and officeholders in the Group ("**Future Options**"). Allocation of the

options to senior officeholders in the Company was also approved by the Company's Audit Committee. The options were granted for no consideration.
Each Option may be exercised into one share, in return for an exercise price equal to NIS 34.85, which is the closing price of the Company's share on the last trading day before the Company Board of Directors' resolution regarding grant of options. It was further resolved that each Future Option granted to future grantees under this grant will be exercisable into one share in return for an exercise price equal to the average closing prices of the Company's shares over the last ten (10) trading days before the Board of Directors' resolution regarding future grant, provided the exercise price of each option for future grant is not less than the par value of the exercisable share. On October 1, 2012 120,000 options were granted to an additional senior officeholder under this grant (out of the Future Options). This grant was also approved by the Compensation Committee and by the Board of Directors, and the exercise price was set at NIS 37.75.
The amounts in the table reflect the benefit component recorded for the options granted under the 2003 Plan, the 2012 Plan and the 2010 Plan (for grants made in 2008 through 2013), as recognized in the Company's 2013 Financial Reports.
For further details regarding the Company's option plans, see Note 12 to the Company's financial statements of December 31, 2013.
[6] Mr. Yehudai has been employed with the Company since 1986, and in 1996 became President and CEO. Mr. Yehudai's terms of employment include monthly salary (index linked), social benefits as is customary in the industry (including managers' insurance, education fund, insurance for loss of work capacity, recuperation pay, sick leave and vacation days), a 13th month salary, ancillaries (including mobile phone, landline at home and newspapers), and a manager's vehicle. In addition, Mr. Yehudai is entitled to an annual bonus as detailed in the Company's Compensation Policy (for further details regarding the Compensation Policy approved see the immediate report on the matter, published on December 29, 2013) and to grant of options according to the Company's option plan, as detailed in sections (7) and (8) below.). Mr. Yehudai's employment may be terminated at the end of 6 months from the date on which the Company notifies of its wish to terminate employment by advance written notice, and 3 months from the date on which Mr. Yehudai notifies the Company of his wish to terminate employment in the Company. In the event a notice of termination is delivered to Mr. Yehudai by the Company within 12 months following the date upon which ICC Handels AG's holdings (directly or indirectly) fall below 26% of the issued and paid up capital of the Company or the voting rights in the Company, the Company shall continue to pay his salary for a period of 12 months beginning on the date of the end of the notice period, save payment for vacations, sick leave, bonuses and options. In this event all options previously granted to Mr. Yehudai under any option plan will also become immediately exercisable, even if their vesting period has not been completed. Upon termination of his employment with the Company, Mr. Yehudai is entitled to receive severance pay equal to two times the severance pay to which he is entitled to under law.
[7] As of December 31, 2013, Mr. Yehudai held 541,057 options exercisable into 541,057 ordinary shares of the Company.
[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 73,261, and the balance of options granted to Mr. Yehudai under the 2010 plan is 458,339. As stated above, starting from 2013, options granted under the 2012 Plan are considered 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 monthly salary, social benefits as is customary in the industry (including managers' insurance, education fund, insurance for loss of work capacity, recuperation pay, sick leave and vacation days), an annual bonus, a mobile phone and a vehicle. In addition, Mr. Anatot is being granted options according to the Company's option plans, as detailed in sections (13) and (14) below. In the event notice of termination is delivered to Mr. Anatot within 12 months following the date upon which ICC Handels AG's holdings (directly or indirectly) fall below 26% of the issued and paid up capital of the Company or the voting rights in the Company, the Company shall continue to pay his salary for a period of 6 months beginning on the date of the end of the notice period, save payment for vacations, sick leave, bonuses and options. In this event all options previously granted to Mr. Anatot will also become immediately exercisable, even if their vesting period has not been completed.

[10] As of December 31, 2013 Mr. Anatot held 144,990 options exercisable into 144,990 ordinary shares of the Company.

[11] As of the date of this report, the balance of options granted to Mr. Anatot under the 2003 Plan is 3,255, the balance of options granted to Mr. Anatot under the 2012 Plan is 22,565 and the balance of options granted to Mr. Anatot under the 2010 Plan is 119,170.

[12] Mr. Granot has been employed with the Company since 2001. Mr. Granot'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 leave and vacation days), a 13th month salary, an annual bonus, ancillaries (including mobile phone, landline at home and newspaper), and a vehicle. In addition, Mr. Granot is being granted options according to the Company's option plans, as detailed in sections (10) and (11) below. Mr. Granot's employment may be terminated with 3 months advance written notice given by either party. In the event notice of termination is delivered to Mr. Granot by the Company within 12 months following the date upon which ICC Handels AG's holdings (directly or indirectly) fall below 26% of the issued and paid up capital of the Company or the voting rights in the Company, the Company shall continue to pay his salary and for a period of 6 months beginning on the date of the end of the notice period, save payment for vacations, sick leave, bonuses and options. In this event all options previously granted to Mr. Granot will also become immediately exercisable, even if their vesting period has not been completed.

[13] As of December 31, 2013, Mr. Granot held 122,329 options exercisable into 122,329 ordinary Company shares.

[14] As at 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 20,577 and the balance of options granted to Mr. Granot under the 2010 plan is 100,000.

[15] Mr. Gill has been employed with the Company since 2006. Mr. Gill'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 leave and vacation days), an annual bonus, a mobile phone and a vehicle. In addition, Mr. Gill is being granted options according to the Company's option plans, as detailed in sections (19) and (20) below. Mr. Gill's employment may be terminated with 3 months advance written notice given by either party.
[16] As of December 31, 2013, Mr. Gill held 65,679 options exercisable into 65,679 ordinary shares of the Company.
[17] As of the date of this report, the balance of options granted to Mr. Gill under the 2003 Plan is 1,722, the balance of options granted to Mr. Gill under the 2012 Plan is 10,623 and the balance of options granted to Mr. Gill under the 2010 Plan is 53,334.
[18] 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.
[19] As of December 31, 2013, Ms. Mirsky held 80,405 options exercisable into 80,405 ordinary shares of the Company.
[20] As of the date of this report, the balance of options granted to Ms. Mirsky under the 2003 Plan is 876, the balance of options granted to Ms. Mirsky under the 2012 Plan is 12,862 and the balance of options granted to Ms. Mirsky under the 2010 Plan is 66,667.

<u>Section (a)(2)</u>
There are no senior officeholders in the corporation who received higher remuneration not included in the above table.

<u>Section (a)(3)</u>
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 2013, which does not deviate from the customary directors' remuneration, came to a total of US$209 thousand.

<u>Section (b)</u>
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 controlling shareholder in the Corporation is ICC Industries Inc., via its subsidiaries. The controlling shareholders of ICC Industries Inc. are Dr. John J. Farber and Ms. Maya Farber.

Regulation 22- Transactions with Controlling Parties

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 2013 or later, through the date of publication of this report or which is still valid at the time of the publication of the report:

Transactions included in Section 270(4) of the Companies Law, 1999 (the "**Companies Law**")

(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) After the balance sheet date, 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.

Transactions not included in Section 270(4) of the Companies Law

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 22 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 February 6, 2014. 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 58,508,845 divided into 58,508,845 shares of NIS 1 par value each.

Issued share capital after deduction of dormant shares: NIS 58,185,662 divided into 58,185,662 shares of NIS 1 par value each.

As of the date of this report the Company holds 323,183 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, 2013 the balance of options existing under the option plan which the Board of Directors adopted in 2003, 2010 and 2012 is 39,101, 1,090,845 and 278,691 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 reports dated December 30, 2013.

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.	113176730 (USA)	113042949 (USA)	453588940 (USA)	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	Chairman of the Board of ICC Industries Inc.	ICC Industries Inc.	Vice-Chair of ICC Industries Inc. and	Served as Director in Frutarom Switzerland Ltd.

director	And serves as Director in ICC Industries Inc. subsidiaries		director in ICC subsidiaries	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., Herzlia	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
Employment over past five years	Business advisor	Chairman of the board of Dash Provident Fund Management Ltd.,	Managing partner at Galram Consultants	Consultant on mergers and acquisitions (2008-2010), member

		Chairman of Yellow Pages Ltd., Chairman of the Bank for Industrial Development Israel Ltd.		of the board of directors at Ormat Industries Ltd.
Names of corporations where serves as director	Served as a director at Retalix Ltd. until Feb. 2013	Yellow Pages Ltd., Elinav Consulting and Services Ltd.; S. Shlomo Holdings Ltd.; Sapiens Ltd.;; Polar Communication Ltd.; Ofer Investments Ltd; Global Box Ltd and A. Dori Group Ltd.	Member of the Management Committee of the Research Fund of Tel Aviv Sourasky Medical Center	Ormat Industries Ltd.
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 office holder	**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	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	VP Teva Europe, Teva Pharmaceuticals

Name of office holder	Ram Pinkhas	Tali Mirsky-Lachman	Guy Gill	Yoav Barak
Position in corporation, subsidiary, related company or interested party	Global Vice President, HR	Global Vice President, Legal Affairs and Corporate Secretary	Vice President Finance. Serves as director in Frutarom subsidiaries.	Internal Auditor
ID no.	058509563	029423837	24223380	53670352
DOB	1964	1972	1969	1955
Year began serving in the company	2013	2010	2006	2004
Independent authorized signatory	No	No	No	No
Interested party in the corporation or relative of senior office holder or of interested party	No	No	No	No
Education	BA, Psychology (Bar-Ilan University) MA Organizational Psychology (Bar-Ilan University)	L.L.B in Law and Business Administration (IDC, Herzelia)	BA in Economics and Accounting (Haifa University)	BA in Economics and Accounting (Haifa University)
Business experience over past five years	Vice President HR, Better Place IL, Vice President HR, Comverse	VP General Counsel and Corporate Secretary at Alvarion Ltd	VP Finance of the Company	Internal auditor for corporations, Chairman of Regba Furniture, Agricultural Cooperative, Internal Auditor for Shemen Industries Ltd., Chairman of Lavi Furniture Industries, Agricultural Cooperative, Director at Fridenzon Logistic Services Ltd.

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 auditors are Kesselman & Kesselman, 1 Nathanson St., Haifa 33034, 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 2013.

Regulation 29 – Recommendations and Resolutions of the Directors and of 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 12, 2013 the Company's Board of Directors resolved on the distribution of dividend of NIS 0.24 per share, totaling NIS 13,997 thousand.

b) After the balance sheet date, 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.

Resolutions of the Extraordinary General Meeting:

c) After the balance sheet date, the Company's general meeting of shareholders held on January 14, 2014 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 the date of appointment by the Meeting, under the terms of directors' engagement as were at 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 the date of appointment by the Meeting, under the terms of directors' engagement existing in 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 controlling shareholders or relatives of such, as detailed in paragraph c to Regulation 22, 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.

Regulation 29A – Company Resolutions

In this matter, see regulation 22 above (transactions with controlling shareholders), the resolution of the Board of Directors under Regulations 29(c) above, and the Company's reports regarding the general meetings of December 29, 2013 and January 14, 2014.

Date: March 18, 2014

Frutarom Industries Ltd.

By:		
Name:	Dr. John Farber	Ori Yehudai
Office:	Chairman of the Board	President and Chief Executive Officer

CHAPTER E

REPORT ON THE EFFECTIVENESS OF THE INTERNAL CONTROLS ON THE FINANCIAL REPORTING AND DISCLOSURE

Annual Report Regarding Effectiveness of Internal Audit on Financial Reporting and on Disclosure

The management of Frutarom Industries Ltd (the "**Corporation)**, supervised by the Corporation's Board of Directors is responsible for prescribing and conducting a proper internal control on the Corporation's financial reporting and disclosure.

For this matter, the members of the 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. Ram Pinhas, Global Vice President, Human Resources
5. Guy Gill, Vice President Finance
6. Tali Mirsky-Lachman, Global Vice President, Legal Affairs and Corporate Secretary
7. Lilit Levi, 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, 2013 is effective.

Acquisition of the PTIPTIVantodio Holdings Limited, holder of the Protein Technologies Ingredients group ("PTI") over the reporting year and reference to FAQ (SOX)

Regarding the description of PTI and the acquisition transaction, see Note 5J to the Company's Periodic Report.
Assessment of effectiveness of internal audit on the financial statement and the disclosure performed by the Company's management under the supervision of the Board of Directors did not include assessment of effectiveness of internal audit on the financial statement and disclosure of PTI.
In accordance with the guidelines of the Securities Authority from July 2010, FAQ (SOX)1, an acquired corporation may be excluded from the assessment of effectiveness of internal audit report until the period report of the year following the year in which control was gained in the acquired corporation.

The reasons for not including the acquired company in the report of assessment of effectiveness of internal audit for this periodic report and the reasons the Company was not able to assess the effectiveness of the acquired company's internal audit as of the date of the report are, in brief, the following:

(A) The date on which the transaction was concluded and the internal audit processes required for implementation – insufficient time had passed for assessment and mapping out internal audit processes existing at PTI from the date on which the transaction was completed until the date of the report, or for full implementation of the Company's internal audit processes at PTI.
(B) Accompanying processes for completion of the transaction – a number of processes were in play for the purpose of the Company's gaining control of the corporation, some complex, relating to handling and organizing work interfaces with the acquired company, creating adaptations and adjustments between the Company's information systems and those of the acquired company, which, in addition to the aforesaid, extended the period required for implementation of the internal auditing process.

In order to assess the effectiveness of PTI's internal audit, the Company, starting from the date on which the acquisition was completed, began examination of the acquired company's existing processes and audits in the matter of financial reporting and disclosure, mapping out risks and identifying material processes.

Manager's Declarations

Declaration of the President and CFO

The undersigned, Mr. Ori Yehudai, hereby declares as follows:

1. I have reviewed the Periodic Report of Frutarom Industries Ltd. (the "**Corporation**") for 2013 (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 Corporationand 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 18, 2014

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 2013 (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 18, 2014

Alon Granot
Executive Vice President and CFO

Annual Report Frutarom

2013

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FRUTAROM INDUSTRIES LTD. 25 HASHAISH STREET POB 10067 HAIFA 2611001, ISRAEL TEL. +972 4 846 2462 FAX +972 4 872 2517 **WWW.FRUTAROM.COM**