

**FRUTAROM INDUSTRIES LTD.
DIRECTORS REPORT TO THE SHAREHOLDERS
FOR THE PERIOD ENDING MARCH 31, 2007¹**

General

Frutarom Industries Ltd. (“Frutarom” or “the Company”), a global company, was established in 1933 and became a public company in 1996 with the registration of its shares for trade on the Tel Aviv Stock Exchange. In February 2005, the Company’s Global Depository Receipts were listed on the London Stock Exchange Official List. Frutarom develops, produces and markets flavors and fine ingredients used to produce food, beverages, flavors, fragrances, pharma/nutraceuticals and personal care products. Frutarom operates production facilities in Europe, North America, Israel and Asia, and produces, markets and sells over 15,000 products to more than 5,000 customers in more than 120 countries. Frutarom operates two divisions: the Flavors Division and the Fine Ingredients Division.

In recent years Frutarom has implemented a strategy for achieving rapid growth, above the industry average, through both internal growth in its core activities and strategic acquisitions. In accordance with this strategy, at the beginning of October 2006 Frutarom acquired 100% of the share equity of the Acatris Health Group, which operates from Holland, Belgium and the United States. After the date of the balance sheet, on April 1, 2007, Frutarom completed the acquisition of 100% of the share equity of Belmay Limited in England in consideration for US\$ 17.1 million. Belmay develops, produces and markets flavors, with a particular focus on natural flavors, for the food and beverage industry. Belmay has subsidiaries in Singapore, Norway and Denmark. In addition, on April 19, 2007, Frutarom acquired 100% of the share equity of the English company Jupiter Flavours Limited, which also develops, produces and markets flavors. In consideration, Frutarom paid US\$ 2.8 million. The acquisition agreement also determines a deferred future payment of up to US\$ 600,000 based on the results Jupiter is expected to achieve.

The Belmay and Jupiter acquisitions join additional acquisitions made by Frutarom in recent years, and contribute to strengthening Frutarom’s activity in Britain and its position as the leading flavors producer in the British market. Belmay’s and Jupiter’s activities are largely synergetic with Frutarom’s activity in Britain and have expanded Frutarom’s product offering to its customers and added new leading customers to Frutarom’s existing customer base in Britain. Frutarom is in the advanced stages of completing the integration of the acquired activities in England in order to achieve the greatest possible operational efficiency and savings, and estimates that this will reach over US\$ 3 million annually. Frutarom persists in investing considerable efforts and resources to implement its strategy for rapid growth in order to strengthen its position as one of the leading global companies in the field of flavors and specialty fine ingredients and to realize its vision, *“To be the Preferred Partner for Tasty and Healthy Success.”*

Frutarom focuses on large multinational customers as well as mid-size and local customers, offering each customer the same superior service and tailor made

¹ Prepared in accordance with the consolidated financial reports of the Company for March 31, 2007, which were prepared in accordance with IFRS.

products. Frutarom concentrates on developed markets such as Western Europe and the United States, as well as fast growing emerging markets such as the CIS, Eastern Europe, Asia, and Latin America, where growth rates are higher than the global average. Frutarom offers its customers a wide product range comprised mostly of natural and innovative, value-added products such as natural functional food ingredients, and continues to invest substantial resources in the Company's research and development activities. As part of these research and development activities and to expand its offering of natural, innovative and unique products, Frutarom is cooperating with universities, research institutes and start-ups in Israel and elsewhere in the world. In the last year, Frutarom initiated several such cooperations: exclusive cooperation with D-Herb, of the NGT technological incubator in Nazareth, Israel, to produce and market a unique herbal extract from the *Portulaca* plant that is used to reduce and stabilize glucose levels in diabetes patients; exclusive cooperation with Magnetika Interactive Ltd., to produce, market and sell products enriched with Omega-3 fatty acid produced from the *Salvia sclarea* plant; and exclusive cooperation with CapsiVit Biotechnology Ltd. to commercialize unique knowhow developed by the Vulcani Institute to produce a natural extract from the *Capsicum annuum L.* plant as a highly bio-available source of carotenoids and particularly capsanthin; and others. These collaborations strengthen and broaden the pipeline of new and innovative products that Frutarom intends to launch in the coming years.

As in the past seven consecutive years, during the first quarter of 2007 Frutarom also achieved growth in sales. Frutarom's sales for the first quarter of 2007 totaled US\$ 80.5 million, growing 13.4% compared with the same quarter of 2006 (sales grew by 10% excluding the impact of the strengthening US dollar against European currencies, in which most of Frutarom's sales are made). Gross profit for the quarter rose 10.2% to reach US\$ 29.8 million, compared with US\$ 27.0 million in the same quarter last year. Gross margin reached 37.0%, compared with 38.1% for the same period last year. Operating profit reached US\$ 10.4 million, similar to the same quarter last year. Operating margin reached 12.9% compared with 14.6% in the same period last year. Profit before tax totaled US\$ 10.1 million compared with US\$ 10.7 million in the same quarter of 2006. Net profit totaled US\$ 7.6 million compared with US\$ 8.8 million for the first quarter last year, when the Company received a one-time tax benefit in the amount of US\$ 1.3 million for previous periods, upon receiving approval as a plant characterized by high technological turnover. Net margin reached 9.5%, compared with 12.5% during the same quarter in 2006, when the one-time tax benefit was recorded.

Profit per share during the first quarter of the year reached US\$ 0.14 compared with US\$ 0.16 during the first quarter of 2006.

Summary of the Company's Activity

Frutarom operates in the global flavors and fine ingredients markets. In the flavors market, Frutarom is active mainly in the segments of flavor compounds and food systems. In the fine ingredients market, Frutarom operates mainly in the segments of natural flavor extracts, natural functional food ingredients, natural pharma/nutraceutical extracts, specialty essential oils, unique citrus products and aroma chemicals.

Leffingwell & Associates estimates the global market for flavors, fragrances and fine ingredients at approximately US\$ 18 billion. Frutarom does not operate in the market for fragrance compounds, 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 had sales of approximately US\$ 15 billion. Based on Leffingwell & Associates' data, Frutarom is ranked as one of the top ten companies in its field for 2006.

According to an estimate published in 2004 by SRI Consultants and IAL Consultants, global sales in the flavor and fine ingredients markets in which Frutarom operates will grow at an annual rate of between 2% and 4% from 2005 to 2008. The growth rate in emerging markets in which Frutarom operates, such as Eastern Europe, Russia, China, India, and South America is expected to be considerably higher due to the expected increases in GNP and changes in consumer preferences in these markets. According to SRI Consultants, the market for functional food ingredients in Europe and the United States is expected to grow at a higher annual rate of 9% in the next several years. Frutarom regards its activity in the functional food ingredients market as an important element in its rapid growth strategy.

The Company's activity is divided into two main divisions, each of which is a major field of activity:

- **The Flavors Division** develops, produces, markets and sells flavor compounds and food systems used mainly by manufacturers of food, beverages and other consumer products. Frutarom develops thousands of different flavors, most of which are tailor-made for specific customers, and continuously develops new flavors in order to meet changing consumer preferences and future customer needs. The Flavors Division (the more profitable of Frutarom's Divisions) has experienced accelerated growth in recent years as a result of both organic growth and the successful integration of a number of strategic acquisitions. The internal growth in the Flavors Division's sales derives mainly from the Division's focus on both developed and emerging markets, to global multinationals as well as mid-sized local customers.
- **The Fine Ingredients Division** develops, produces, markets and sells natural flavor extracts, natural functional food ingredients, natural pharma/nutraceutical extracts, specialty essential oils, unique citrus products, aroma chemicals, and natural gums and stabilizers. The Division's products are sold principally to the food, beverage, flavor and fragrance, pharma/nutraceutical and personal care industries. The Fine Ingredients Division has experienced growth in recent years as a result of both internal growth and several strategic acquisitions. The internal growth in the Fine Ingredients Division's sales is mainly the result of the development of new, innovative value-added products with higher than average

margin and its focus on multinational, mid-sized and local customers worldwide. Most of the Division's products are natural products, which enjoy a higher demand than non-natural products. Frutarom acts to expand the natural product portfolio it offers to its customers, with particular emphasis on the functional food area.

Frutarom will continue to focus on implementing its rapid growth strategy that it has successfully implemented in recent years in order to strengthen its positioning as one of the leading global companies in the field of flavors and fine ingredients.

Results of Activity in the First Quarter of 2007

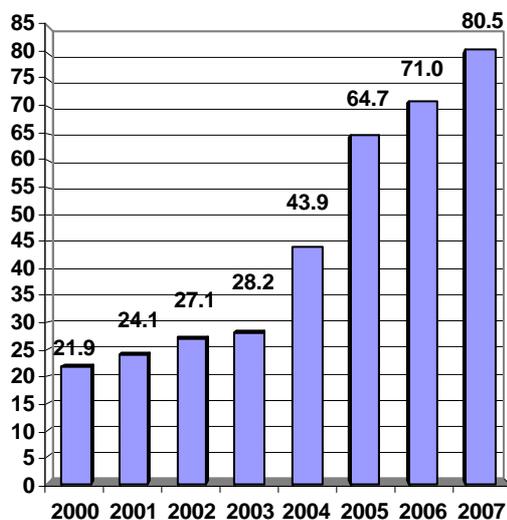
Following is a summary of the profit and loss report for the first quarter (US\$ millions):

	2007	2006	Change (%)
Sales	80.5	71.0	13.4%
Gross profit	29.8	27.0	10.2%
R&D, Selling, Administration, General and Other income	19.4	16.7	16.5%
Operating profit	10.4	10.4	0.1%
EBITDA	13.3	13.1	1.3%
Profit before tax	10.1	10.7	-5.1%
Net profit	7.6	8.8	-13.8%

Sales

Frutarom's sales during the first quarter of 2007 totaled US\$ 80.5 million, showing growth of 13.4%, compared with the same quarter of 2006, when sales totaled US\$ 71.0 million. Sales grew by 10%, excluding the impact of the strengthening US dollar against European currencies (in which most of Frutarom's sales are made).

Sales Development in the First Quarters of 2000-2007 (US\$ millions)



The increase in sales during the quarter was influenced mainly by the following factors:

- A. Growth in the sales of flavors produced and sold by the Flavors Division.
- B. The integration of Acatris's activity, which was acquired and consolidated as of October 2006 with the Frutarom Group's global activity.
- C. Utilizing the synergy and cross selling opportunities between Frutarom's Divisions, existing customers and products and those added through the acquisitions made in recent years.
- D. The strengthening of the European currencies (in which most of Frutarom's sales are made) against the dollar.

Sales Breakdown by Fields of Activity in the First Quarters of 2000–2007 (in US\$ millions and in %)

		2000	2001	2002	2003	2004	2005	2006	2007
Flavors Division	Sales	6.8	9.0	10.8	12.7	20.3	40.3	44.7	49.9
	%	31.1%	37.3%	39.9%	45.0%	46.2%	62.3%	63.0%	62.0%
Fine Ingredients Division	Sales	13.8	13.9	14.9	14.2	22.5	23.4	25.5	29.1
	%	63.0%	57.7%	55.0%	50.4%	51.3%	36.2%	35.9%	36.2%
Trade & Marketing	Sales	1.7	1.5	1.6	1.8	1.7	1.8	1.4	2.6
	%	7.8%	6.2%	5.9%	6.4%	3.9%	2.8%	2.0%	3.2%
Inter Division	Sales	-0.4	-0.3	-0.2	-0.5	-0.6	-0.8	-0.6	-1.1
	%	-1.8%	-1.2%	-0.7%	-1.8%	-1.4%	-1.2%	-0.9%	-1.4%
Total Sales		21.9	24.1	27.1	28.2	43.9	64.7	71.0	80.5

Gross Profit

Gross profit grew 10.2% during the first quarter of 2007 to reach US\$ 29.8 million, compared with US\$ 27.0 million in the same quarter of 2006. Gross margin reached 37.0% during the period, compared with 38.1% during the same period in 2006. Frutarom continues working to adjust the selling prices of its products to the price increase in raw materials used in the production of these products to improve gross margin.

Selling, Marketing, Research and Development, Administration, General and Other Expenses

Selling, marketing, research and development, administration, general and other expenses totaled US\$ 19.4 million (24.1% of sales) in the first quarter of 2007, compared with US\$ 16.7 million (23.5% of sales) during the same period of 2006. The growth in expenses is in part due to the addition of the Acatris activity, which was acquired in October 2006, the growth in the scope of activity and to one time

expenses recorded in the first quarter for the implementation of the ERP system at the Company's sites in Israel and Switzerland.

Operating Profit

Operating profit totaled US\$ 10.4 million in the first quarter of 2007, similar to the same quarter of 2006. Operating margin for the report period reached 12.9%, compared with 14.6% during the same period in 2006.

Finance Expense/Income

Finance expense for the first quarter of 2007 totaled US\$ 0.2 million (0.3% of sales), compared with income of US\$ 0.3 million (0.4% of sales) in the same period in 2006.

Profit before Tax

Profit before tax for the first quarter of 2007 reached US\$ 10.1 million (16.2% of sales), compared with US\$ 10.7 million (15.1% of sales) during the same period in 2006.

Taxes on Income

Taxes on income in the first quarter of 2007 totaled US\$ 2.5 million (24.8% of profit before tax), compared with US\$ 1.8 million (17.2% of profit before tax) during the same period in 2006, when the Company received a one-time tax benefit in the amount of US\$ 1.3 million for previous periods upon receiving approval as a plant characterized by high technological turnover.

Net Profit

Net profit for the first quarter of 2007 reached US\$ 7.6 million, compared with US\$ 8.8 million in the first quarter of 2006. Net margin totaled 9.5%, compared with 12.5% in the same quarter in 2006, when the aforementioned one-time tax benefit was recorded.

Summary of quarterly profit and loss (US\$ millions):

	Q1 2006	Q2 2006	Q3 2006	Q4 2006	Q1 2007
Sales	71.0	72.3	71.3	72.6	80.5
Gross profit	27.0	26.3	26.9	25.7	29.8
Selling, Marketing, R&D, Administration, General and Other income	16.7	16.6	17.7	17.9	19.4
Operating profit	10.4	9.7	9.2	7.8	10.4
EBITDA	13.1	12.5	11.8	11.4	13.3
Finance expenses	-0.3	0.6	0.1	0.1	0.2
Profit before tax	10.7	9.1	9.2	7.7	10.1
Net Profit	8.8	8.6	7.0	5.3	7.6

Frutarom's business is subject to seasonal fluctuations, generally with higher sales and profitability (due to product mix) in the first half of a given year and lower sales and profitability during the second half of a given year. A substantial portion of the

Company's products are used by its customers in the manufacture of beverages and dairy products such as soft drinks, ice cream and yogurts, for which demand generally increases during the summer months. As a result, sales of certain flavors and fine ingredients produced by Frutarom rise in the first half of the year, as manufacturers of beverages and dairy products restock their inventories and increase production in advance of rising demand during the summer months.

The impact of seasonality on the Company's results has weakened in recent years as the Company has increased its sales of products such as savory flavors, natural functional food ingredients, and natural pharma/nutraceutical extracts, which are intended for the pharma/nutraceutical industries and generally have lower seasonality in demand. A major portion of Nesse's sales (Frutarom acquired 70% of Nesse's share capital in January 2006) are intended for the savory field and thus also reduce the effect of seasonality. The products of Acacris Health, whose acquisition was completed at the beginning of October 2006, are also expected to contribute to modifying the seasonality of sales.

Financial Status

Total assets on March 31, 2007 amounted to US\$ 343.5 million, compared with US\$ 271.3 million at March 31, 2006 and US\$ 316.7 million at December 31, 2006.

The Company's current assets totaled US\$ 173.8 million, compared with US\$ 134.1 million at March 31, 2006, and US\$ 149.1 million at December 31, 2006.

Non current assets totaled US\$ 169.7 million on March 31, 2007, compared with US\$ 137.2 million at the end of the first quarter of last year and US\$ 167.6 million at December 31, 2006.

The growth in overall assets, and particularly in current assets, resulted mainly from the addition of the Acacris assets following their acquisition in October 2006 and the growth in activity.

Liquidity

Current activities during the first quarter of 2007 consumed a cash flow of US\$ 2.7 million, compared with the first quarter of 2006, when current activities generated a cash flow of US\$ 3.6 million. The decrease in cash flow resulted from the growth in sales during the first quarter compared with the sales of the fourth quarter of 2006, and from tax payments for previous years.

Sources of Finance

Sources of the Company's Shareholders' Equity

The Company's shareholders' equity at March 31, 2007 totaled US\$ 223.6 million (65.1% of the balance sheet), compared with US\$ 186.1 million (68.6% of the balance sheet) at March 31, 2006. Most of the increase in shareholders equity resulted from the net profit achieved during the period. A change in the US dollar exchange rate against other currencies that are the main activity currency for the autonomous subsidiaries influenced the "currency translation differences equity fund" and increased the shareholders' equity balance. This item does not affect the profit and loss and the cash flow.

Short-Term Loans (Quarterly Average)

Short term credit from banks during the first quarter of 2007 totaled US\$ 1.8 million. During the same period last year, the Company had US\$ 0.4 million at its disposal. At the end of the quarter, the Company took a loan in the amount of US\$ 16.7 million for the acquisition of Belmay Limited.

Credit from Suppliers and to Customers (Quarterly Average)

During the first quarter of 2007 the average scope of credit from suppliers and other creditors was US\$ 55.9 million (compared with US\$ 42.8 million during the same quarter of 2006). During the first quarter of 2007, the Company granted average credit of US\$ 59.5 million to its customers, compared with US\$ 51.8 million during the same quarter of 2006. Most of the growth in suppliers' and customers' credit results primarily from the acquisition of Acatris and the growth in activity compared with 2006.

Distribution of Dividend

On March 19, 2007, the Board of Directors of the Company declared the distribution of a cash dividend at the rate of NIS 0.18 per share, totaling NIS 10.4 million. The dividend was distributed on May 1, 2007.

Disclosures about Market Risk

The Company's activity is characterized by significant dispersal. Through its two Divisions, 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 Company is not significantly dependent on any of its customers, products or suppliers.

The Company operates in a multi-currency environment. Currency exposure is reviewed as needed, on at least a quarterly basis. The Company does not generally take external hedging actions or use other financial instruments for protection against currency fluctuations. The Company's Chief Financial Officer is responsible for managing market risks as relates to exchange rates and interest. 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.

The Managers of the two Divisions are responsible for managing market risk as it relates to changes in raw material prices. 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.

There were no significant changes relating to market exposure and their management during the first quarter of 2007.

Peer Review of the Auditors' Work

In accordance with the instructions of the Securities Authority of July 28, 2005, regarding the disclosure of consent to perform a peer review whose goal, according to the stated instructions, is to put in place a process of control on the audit work performed by the auditor, which will contribute to the existence of an advanced capital market, the Company agreed to the transfer of the information required to perform a sampling related to the peer review. The Company's consent was given subject to obtaining the auditor's commitment according to which before beginning a review of the material relating to the Company, the Company's auditor will certify that the accountants performing the review commit to maintaining all material transferred to them as part of the peer review procedure in confidence and to avoid any situation of conflict of interests.

Events Following the Balance Sheet Date

Acquisition of Belmay

On March 28, 2007, Frutarom, through its subsidiary, Frutarom (UK) Ltd., signed an agreement to acquire 100% of the share capital of the British company Belmay Limited, which has subsidiaries in Singapore, Norway and Denmark, in consideration for a payment of US\$ 17.1 million. Belmay's sales for 2006 totaled US\$ 15.1 million. The acquisition was completed on April 1, 2007.

Belmay is a leading British flavor house that develops, produces and markets flavors, with a particular focus on natural flavors, for the food and beverage industry. Belmay has a site with significant production capacity that is located close to Frutarom's production site in Kettering, England, which adheres to the most stringent standards in the food and beverage industry in Europe. Belmay employs some 85 employees. Belmay's extensive customer base includes leading food and beverage manufacturers in its countries of operation.

The acquisition of Belmay is an important strategic acquisition that makes Frutarom the leading flavor house in the British market and enhances its presence and position in additional important target markets. Belmay's acquisition significantly strengthens Frutarom's technological capabilities and the product portfolio it offers its customers in the flavors field, especially in soft drinks and alcoholic beverages. The acquisition further supports Frutarom's position, which is already one of the ten largest companies in the world in its field.

Acquisition of Jupiter

On April 19, 2007, Frutarom, through its subsidiary, Frutarom (UK) Ltd., signed an agreement to acquire 100% of the share capital of the British company Jupiter Flavours Limited, which develops, produces and markets flavors.

In consideration, Frutarom made a cash payment of US\$ 2.8 million. The acquisition agreement also determines a deferred future payment of up to US\$ 600,000 based on the results Jupiter is expected to achieve. Jupiter showed high growth rates over the past few years and its sales volume for the twelve month period preceding the acquisition was approximately US\$ 2 million.

The activities of Belmay and Jupiter are highly synergetic with the activity of Frutarom's Flavors Division, particularly in the English market. Frutarom is in the advanced stages of completing the integration of the acquired activities in England into one site in order to achieve the greatest possible operational efficiency and savings, and estimates that this will reach over US\$ 3 million annually. Uniting the activities will contribute to extraction of the many cross selling opportunities existing between the acquired activities and that of Frutarom.

The Board of Directors of the Company held two meetings during the first quarter of the year.

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

Dr. John J. Farber
Chairman of the Board

Ori Yehudai
President & CEO

May 20, 2007