FRUTAROM INDUSTRIES LTD.
DIRECTORS' REPORT OF THE COMPANY'S BUSINESS
FOR THE PERIOD ENDING SEPTEMBER 30, 2012

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. The Company and its subsidiaries (**"Frutarom"** or the **"Group"**) develop, produce and market flavors and fine ingredients used in the manufacture of food, beverages, flavors, fragrances, pharmaceuticals/nutraceuticals and personal care products. Frutarom operates production facilities in Europe, North America, Latin America, Israel, Asia and Africa, markets and sells over 30,000 products to more than 14,000 customers in more than 130 countries and employs some 2,050 people throughout the world.

Frutarom operates in two major segments: the Flavors segment and the Specialty Fine Ingredients segment.

- **The Flavors Segment -** Frutarom develops, produces, markets and sells sweet and savory flavor solutions, including flavors extracts and products which in addition to flavor extracts also contain fruit or vegetable ingredients and other natural ingredients ("food systems"), which are used mainly in the manufacture of foods, beverages and other consumer products. Frutarom develops thousands of different flavors for its customers, most of which are tailor-made and customized for specific customers, and consistently develops new products to meet changing consumer preferences and future customer needs.

  In recent years, Frutarom's Flavors' segment has undergone accelerated growth, and it currently constitutes 73% of Frutarom's total sales (compared with 40% in 2001). This accelerated growth is the result of a focus on the rapidly growing market of natural flavors; development of unique, cutting edge product solutions combining taste and health offered to the large multi-national sector; focus on mid-size and local customers in emerging and developed markets (focusing in particular on private labels), the provision of customized services, including technological and marketing support and assistance in the development of products and the provision of high level tailor-made services and products, at the levels they are normally provided for large multi-national companies; and a result of Frutarom's strategic acquisitions, some of which already have and others of which are in the process of being successfully incorporated into Frutarom's global activities.

- **The Specialty Fine Ingredients Segment -** Frutarom develops, produces, markets and sells natural flavor extracts, natural functional food ingredients, natural pharmaceutical/nutraceutical extracts, aroma chemicals, essential oils, unique citrus products, and natural gums and stabilizers. The Specialty Fine Ingredients products are sold primarily to the food, beverage, flavor, fragrance, pharmaceutical/nutraceutical and personal care industries.

  The Specialty Fine Ingredients segment focuses on a value-added product portfolio, which gives Frutarom a competitive edge. Most of the specialty fine ingredients are natural products which enjoy higher than average demand compared with non-natural products. Frutarom is constantly expanding the natural product portfolio it offers its customers, focusing on an extensive variety of natural, functional and healthy products.

RAPID GROWTH STRATEGY – PROFITABLE ORGANIC GROWTH AND STRATEGIC ACQUISITIONS

Frutarom relentlessly implements its rapid profitable growth strategy, strengthening its research and development, manufacturing, marketing and sales infrastructures and continually seeking out additional strategic acquisitions.

Over the last ten years, Frutarom has grown at an average yearly rate of 17%, through a combination of organic growth and the 23 acquisitions it made over this period. Company revenues over this period grew from revenues of approximately US$100 M and net profit of US$4 M in 2001 to revenues of US$518.4 M and net profit of US$42 M in 2011. This rapid and profitable growth trend continued over the first nine months of 2012, bringing about record sales of US$473.1 M and a record net profit of US$41.4 M.

The successful implementation of rapid strategic growth has allowed Frutarom to significantly expand its activities in the Flavors segment, its most profitable segment, which now represents 73% of total Frutarom sales compared with 40% of total sales ten years ago, while achieving organic growth at a higher rate than the market growth in the markets it operates in.

The Company is confident that the rapid growth trend will continue even under today's challenging market conditions.

- Emerging markets – The realization of Frutarom's strategy of accelerated expansion into target markets with higher growth rates is reflected in the 70% increase in dollar terms achieved over the first nine months of 2012 in the emerging markets of China and Southeast Asia, Central and South America, Central and Eastern Europe and Africa. The sales segment in these markets grew from 25% in the first nine months of 2010 to 35% in the first nine months of the year. In the BRIC countries, Frutarom's sales this year grew by 41% in dollar terms. The results of the first nine months also reflect the continued rapid growth of the Flavors' activities in North America, the largest flavors market in the world, which grew by 60% in dollar terms.

  Frutarom continues to invest great resources and focuses on accelerating its expansion and increasing its market share in these markets and to utilize the full potential and commercial opportunities existing in these markets.

- Acquisitions and mergers - Frutarom has vast experience in mergers and acquisitions, and it consistently acts to integrate acquired companies and activities into its existing activities, utilizing both commercial and operational synergies to optimize cross-selling opportunities, cost savings and improvement of profit margin.

After seven acquisitions in 2007 and three in 2009, all of which were successfully integrated into its global activities and contribute to a growth in sales and improved margins, Frutarom has continued its acquisition strategy and made five additional strategic acquisitions in 2011 and three in the first quarter of 2012. The acquisition of the Slovenian company Etol Tovarna arom in eteričnih olj d.d ("Etol") was completed on June 5, 2012. The total cost of the acquisition came to €35.4 M.

Integration of the eight acquisitions is moving ahead successfully and according to plan, and the acquired activities have contributed in this quarter as well not only to growth in sales but also to improved profit. As integration progresses and the many synergies are realized, contribution to profit will increase and mainly come to fruition next year. In addition, Frutarom is working towards the integration of production sites and activities as well as the transfer of some activities to countries where operating costs are lower, with the aim of achieving additional significant savings which will come to fruition mainly starting from the second half of the coming year.

- Taste and Health - Frutarom is developing innovative tailor-made taste and health solutions. The solutions provided by the Company are in line with major trends of the global food market and with consumer demand, including bringing together taste and health, developing health supplements, anti-aging products and foods targeting specific populations and age groups. The added value which Frutarom offers its customers and Frutarom's unique capabilities to combine taste solutions with raw materials of added health value, give the Company an important competitive advantage with customers in both emerging and matured markets.

It is Frutarom's assessment that its capital structure (total assets of US$768.1 M and equity of US$434.7 M as of September 30, 2012, constituting 56.6% of the total balance sheet) and its net debt level (total loans after deduction of cash) of US$152.2 M as of September 30, 2012, supported by the cash flow it achieves, and together with bank backing, will allow it to continue to realize its acquisition strategy as it has done over the past few years while strengthening its 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 at September 30, 2012 totaled US$768.1 M compared with US$612.2 M as at September 30, 2011 and US$650.0 M as at December 31, 2011.

The Group's current assets totaled US$299.9 M, compared with US$ 247.0 M as at September 30, 2011 and US$246.6 M as at December 31, 2011.

Net fixed assets after deduction of accumulated depreciation and other assets as at September 30, 2012 totaled US$464.9 M compared with US$363.0 M as at September 30, 2011 and US$401.2 M as at December 31, 2011.

The increase in total assets was mainly affected by the eight acquisitions completed in 2011 and during the first quarter of 2012 offset by exchange differentials of values of subsidiary assets with operating currencies other than the dollar, following the weakening of the exchange rates of European currencies and the NIS, except the Pound Sterling versus the US dollar as at September 30, 2012, compared with September 30, 2011.

C. RESULTS OF OPERATIONS IN Q3 2012

In Q3 2012 Frutarom achieved a third quarter record high in sales, gross profit, operational profit, EBITDA, net profit and earnings per share, and showed a substantial improvement in cash flow, despite challenging market conditions in the global economy in general and in Western Europe in particular and despite the strengthening of the dollar versus the main currencies in which the Company operates, which detracted from dollar sales and profits.

Frutarom sales over Q3 2012 grew by 26.0%, net of currency effects, reaching a third quarter sales record high of US$157.1 M, compared with US$135.3 M for the same quarter last year. Cash flow from operating activities rose by 37.1% reaching US$22.7 M, compared to cash flow of US$16.6 M during the same quarter last year.

The trend of improvement in profit and gross and operational margins continues. Gross margin increased and achieved 37.0% in Q3, compared with 35.2% in the same quarter last year. Net of Etol's trade and marketing activity (a non-core activity for Frutarom), gross margin rate over the quarter increased, reaching 38.1%. The improvement in profit and gross margin was driven by a combination of adjustments in Frutarom's product selling prices to its customers, continued stabilization and even the start of a decrease in the prices of some of the raw materials Frutarom uses in the manufacture of its products, the actions taken for lowering raw materials costs by strengthening global purchase and utilization of the many operational synergies derived from the recent acquisitions - actions whose results are expected to come more fully to fruition over the course of next year.

Frutarom consistently acts to integrate its new acquisitions with existing activities, and capitalizing on increased synergies and new cross-selling options deriving from the eight acquisitions made over 2011 and the first quarter of 2012.

The integration of sales, marketing, research and development, purchasing and production activities of the eight acquisitions are progressing successfully and as planned. Over Q3 these acquisitions contributed not only to a growth in sales but also to improved profit. As integration progresses and the many synergies achieved from the acquisitions are realized, their contribution to profits will increase, an increase which will mainly come to fruition in 2013.

In addition, Frutarom is moving ahead with plans to integrate a number of production sites and transferring other activities to countries where operational costs are lower. The contribution of these activities will come to fruition mainly starting from the second half of 2013.

Frutarom estimates that continued internal growth, together with a combination of stabilization and the beginning of a decrease in the prices of raw material and the impact of the Company's updated selling prices, the continued realization of streamlining processes and improved costs structure, with maximum utilization of production sites throughout the world and successful integration of recent acquisitions will bring about improved future margins and continued strengthening of Frutarom's competitive advantage and its positioning as one of the leading companies in the world in the fields of taste, health and fine ingredients.

Sales

Frutarom's sales in Q3 2012 increased by 24.0%, net of currency effects, reaching a third quarter record high of US$157.1 M, compared with US$135.3 M during Q3 2011, despite challenging market conditions throughout the world and particularly in Western Europe. Currency effects detracted 7.8% (US$10.6 M) from growth in sales due to the strengthening of the average exchange rate of the US dollar versus European currencies and the NIS in Q3 of last year, thus in dollar terms, sales grew by 16.2%. The acquisitions made after August 1, 2011 and in Q1 2012 contributed US$28 M to sales during this quarter. Organic growth (net of the contribution of the acquisitions and currency effects) reached 3.3% this quarter.

Frutarom's sales in the Flavors segment grew by 26.4%, net of currency effects, compared with the same quarter last year, reaching a third quarter record high of US$114.2 M. The acquisitions made after August 1, 2011 and in the first quarter of 2012 contributed US$23 M to Flavor segment sales this quarter. Organic growth in the Flavors segment (net of the contribution of the acquisitions and currency effects) reached 3.1% this quarter. Sales in the Flavors segment already constitute 73% of total Frutarom sales, compared with 40% in 2001.

Frutarom sales in the Specialty Fine Ingredients segment increased by 4.5%, net of currency effects, compared with the same quarter last year, reaching US$37.2 M.

Frutarom sales in Trade and Marketing increased by US$5.1 M compared with the same quarter last year, reaching US$6.3 M. Growth in sales derived from the inclusion of Etol's activities in this field, which contributed US$5 M to sales this quarter.

Sales breakdown by segments in Q3 in 2002 - 2012 (US$ M and %)

		Q3 2002	Q3 2003	Q3 2004	Q3 2005	Q3 2006	Q3 2007	Q3 2008	Q3 2009	Q3 2010	Q3 2011	Q3 2012
Flavor Segment	**Sales**	11.8	21.1	28.1	36.2	47.2	57.6	86.1	77.3	75.4	96.9	114.2
	%	42.8%	49.8%	54.7%	61.0%	66.3%	65.7%	71.7%	69.3%	67.9%	71.7%	72.7%
Fine Ingredient Segment	**Sales**	14.7	20.3	22.1	22.7	23.9	28.1	31.1	33.5	34.6	37.8	37.2
	%	53.4%	48.0%	43.0%	38.2%	33.6%	32.0%	25.9%	30.1%	31.1%	27.9%	23.7%
Trade & Marketing	**Sales**	1.5	1.6	1.8	1.6	1.8	3.3	3.8	1.5	1.5	1.3	6.3
	%	5.4%	3.7%	3.5%	2.8%	2.5%	3.7%	3.2%	1.3%	1.4%	1.0%	4.0%
Inter Segments	**Sales**	-0.5	-0.6	-0.6	-1.1	-1.7	-1.3	-1.0	-0.7	-0.5	-0.7	0.6-
	%	-1.6%	-1.5%	-1.2%	-2.0%	-2.4%	-1.4%	-0.9%	-0.7%	-0.5%	-0.5%	0.4%-
Total Sales		27.5	42.4	51.4	59.4	71.3	87.7	120.0	111.6	111.0	135.3	157.1

The following is a summary of the profit and loss reports for Q3 2011 – 2012 (US$ M):

During Q3 2012 Frutarom achieved third quarter record highs in sales, in gross, operating, EBITDA and net profits and earnings per share, despite the strengthening of the dollar versus the main currencies in which it operates (European currencies and the NIS), which detracted from sales and profits in dollars.

	Q3 2011	Q3 2012	Difference between 2011 – 2012 (%)
Sales	135.3	157.1	16.2%
Gross profit	47.7	58.1	21.8%
R&D, Selling, Administration, General and Other expenses	34.8	38.5	10.8%
Operating profit	12.9	19.5	51.5%
EBITDA	18.6	26.3	41.7%
Pretax profit	10.3	18.9	84.5%
Financing expenses(income)	2.6	0.6	-77.5%
Net profit	8.7	14.4	66.0%

Gross Profit

The Company's gross profit in Q3 2012 increased by 21.8%, reaching a third quarter record high of US$58.1 M compared with US$47.7 M during the same quarter last year. Gross margin net of Etol's trade and marketing activity (a non-core activity of Frutarom) increased, achieving 38.1% compared with gross margin of 35.2% during the same period in 2011. Gross margin including Etol's trade and marketing activity also increased, reaching 37.0%.

Organic growth in sales, the combination of updating Frutarom's selling prices to its customers, continued stabilization in the prices of some of the raw materials Frutarom uses for the manufacture of its products, the actions Frutarom takes in order to maximize potential for lowering raw material costs by strengthening global purchase, and the start of the impact of utilization of the many operational synergies from the recent acquisitions, whose main impact is not yet seen in the Company's results, all contributed to the improvement in gross profit and margin.

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

In Q3 2012 selling and marketing, research and development, general and administrative and other expenses totaled US$38.5 M (24.5% of sales), compared with US$34.8 M (25.7% of sales) during the same quarter last year.

Over Q3 2011 selling and marketing, research and development, general and administrative expenses included one-time expenses for acquisitions in the amount of US$1.3 M.

Increased expenses were the result of a growth in the scope of activity, and primarily deriving from the acquisitions made in 2011 and over the first quarter of 2012.

Frutarom acts for the continued achievement of maximum efficiency, for the improvement of its cost structure and the strengthening its future competitiveness, while maximally utilizing its manufacturing sites throughout the world and its successful integration of its latest acquisitions.

As mentioned, in addition to the many cross-selling opportunities, the acquisitions also created many opportunities for profit and margin improvement, due to the integration of sales, marketing and R&D, optimization of production, supply and logistics, and improvement of global purchasing capacity and strengthening purchase sources. In addition, Frutarom is working towards the realization of a number of plans for integration of production sites and activities and the transfer of other activities to countries where operating costs are lower, anticipated to expand profits and margins mainly starting from the second half of next year.

Operating Profit and EBITDA

In Q3 2012, operating profit increased by 51.5%, reaching a third quarter record high totaling US$19.5 M (12.4% of sales) compared with US$12.9 M (9.5% of sales) during the same quarter last year.

The EBITDA achieved by Frutarom in Q3 2012 increased by 41.7% reaching a third quarter record high of US$26.3 M (16.7% of sales), compared with US$18.6 M during the same period last year (13.7% of sales).

Finance Expenses / Income

In Q3 2012, financing expenses totaled US$0.6 M (0.4% of sales), compared with financing expenses of US$2.6 M (1.9% of sales) during Q3 2011.

Interest expenses during Q3 2012 reached US$1.7 M compared with US$0.4 M during the same quarter last year. The increase in interest expenses is due to the increase in the Company's loans in light of the acquisitions made.

Financing income from exchange differentials totaled US$1.1 M compared with financing expenses which came to US$2.2 M during the same quarter last year. The increase in financing income deriving from exchange rates is due to the weakening of the dollar exchange rate, mainly versus European currencies and the Israeli shekel as of September 30, 2012, compared with the exchange rate of the dollar versus those same currencies at June 30, 2012.

Pretax profit

In Q3 2012 pretax profit increased by 84.5%, reaching a third quarter record high of US$18.9 M (12.0% of sales) compared with US$10.3 M in Q3 2011 (7.6% of sales).

Taxes on Income

In Q3 2012, taxes on income totaled US$4.5 M (23.9% of pretax profit) compared with US$1.6 M in Q2 2011 (15.4% of pretax profit).

The low tax rate in Q3 2011 is mainly due to income from taxes for previous years in the amount of US$1.0 M (net of such aforesaid tax income the tax rate for Q3 2011 stood at 25.2%).

Net Profit

In Q3 2012, net profit increased by 66% reaching a quarterly record high of US$14.4 M compared with US$8.7 M in Q3 2011. Net margin totaled 9.2% compared with 6.4% during the same quarter last year.

Earnings per Share

In Q3 2012, earnings per share reached a quarterly high of US$0.25 per share, compared with US$ 0.15 in the same quarter last year.

Summary of the quarterly profit and loss reports for 2009 - 2012 (US$ M):

	Q1 2009	Q2 2009	Q3 2009	Q4 2009	Q1 2010	Q2 2010	Q3 2010	Q4 2010	Q1 2011	Q2 2011	Q3 2011	Q4 2011	Q1 2012	Q 2 2012	Q 3 2012
Income	98.4	106.7	111.6	108.5	113.5	114.3	111.0	112.4	121.0	130.6	135.3	131.6	151.2	164.8	157.1
Gross profit	35.2	39.4	41.2	39.6	43.5	46.9	43.2	41.3	45.7	48.5	47.7	46.8	54.9	61.8	58.1
Selling, Marketing, R&D, General and Administrative, and Other Expenses	25.0	26.7	27.9	28.6	26.9	27.5	28.2	29.2	29.0	31.5	34.8	34.6	37.1	40.0	38.5
Operating profit	10.2	12.8	13.3	11.0	16.6	19.4	15.0	12.1	16.6	17.0	12.9	12.2	17.8	21.8	19.5
EBITDA	14.5	17.4	18.3	16.0	21.3	24.0	19.8	16.9	21.5	22.2	18.6	18.1	25.0	28.5	26.3
Finance expenses	3.3	0.1	0.0	0.9	1.3	2.3	-0.2	-0.2	-0.9	0.8	2.6	3.2	0.9	4.3	0.6
Pretax profit	6.9	12.7	13.2	10.1	15.3	17.1	15.2	12.2	17.5	16.2	10.3	8.9	16.9	17.5	18.9
Net profit	5.6	10.1	10.0	7.5	11.1	13.0	11.1	8.8	13.1	12.3	8.7	7.9	13.5	13.5	14.4

Frutarom's business is characterized by seasonal fluctuations, generally expressed by higher sales and margin in the first half of a given year, with lower sales and margin during the second half, mainly in the fourth quarter. The seasonality is a result of the fact that a substantial portion of the Company's products are used by its customers in the manufacture of beverages, ice cream and yogurt, for which demand increases during the summer months. As a result, sales of certain flavor solutions and fine ingredients produced by the Company tend to increase in the first half of the year as beverage, ice cream and yogurt manufacturers restock their inventories and increase production in advance of rising demand during the summer months. The seasonality effect on the Company's results and activity has moderated over recent years with the significant increase in sales of savory products following the acquisitions of companies and activities in this field. The increase in the sales of natural functional food ingredients and natural pharmaceutical/nutraceutical extracts, intended for the pharmaceutical/nutraceutical industries, also contributes to a lower seasonality effect.

D. RESULTS OF OPERATIONS IN THE FIRST 9 MONTHS OF 2012

Sales

Over the first nine months of 2012, Frutarom's sales grew by 27.9%, net of currency effects, achieving record sales for the first nine months of US$473.1 M, versus US$386.9 M during the first nine months of 2011, despite challenging market conditions throughout the world and primarily in Western Europe. Currency effects detracted 5.6% (US$21.6 M) from growth in sales, due to the strengthening of the exchange rate of the US dollar versus the exchange rates of European currencies and the NIS, thus in dollar terms, sales grew by 22.3%. The acquisitions made in 2011 and in Q1 2012 contributed US$98 M to sales during this period. Organic growth (net of the contribution of the acquisitions and currency effects) reached 2.6% over the first nine months of the year.

Frutarom's sales in the Flavors segment, net of currency effects, increased by 34.6% compared with the first nine months of last year, reaching a record high of US$345.6 M, constituting 73.0% of Frutarom's total sales.

Accelerated growth in the Flavor segment, Frutarom's most profitable activity, derives from internal growth at rates above growth rates in the markets Frutarom operates in and in strategic markets in which Frutarom has invested great resources for acceleration of growth, mainly in North America, Latin America, Asia, Africa and Central and Eastern Europe, and from the acquisitions made in 2011 and the first quarter of 2012 in Flavors, which contributed US$84 M to sales for the first nine months of 2012. Organic growth in the Flavors segment (net of the contribution of the acquisitions and currency effects) reached 3.5% over the first nine months of the year.

Frutarom sales in the Specialty Fine Ingredients segment grew by 1.1%, net of currency effects, compared with the first nine months last year, reaching US$111.2 M.

Frutarom sales in Trade and Marketing increased by US$12.8 M compared with the first nine months of last year, reaching US$18.0 M. Sales included Etol's activities in this field, which contributed US$14 M sales over the first nine months of 2012.

Sales Breakdown by Segments in the first nine months of 2002-2012 (US$ M and %)

		2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Flavor Segment	**Sales**	34.9	49.7	70.8	119.6	141.5	169.2	268.6	220.4	228.2	269.8	345.6
	%	41.6%	48.3%	50.6%	62.5%	65.9%	65.1%	71.7%	69.6%	67.4%	69.7%	73.0%
Fine Ingredient Segment	**Sales**	45.6	49.8	65.6	69.8	72.0	86.1	98.9	92.9	108.3	114.1	111.2
	%	54.3%	48.4%	46.9%	36.5%	33.5%	33.1%	26.4%	29.3%	32.0%	29.5%	23.5%
Trade & Marketing	**Sales**	4.7	5.1	5.3	5.0	4.7	7.9	10.4	5.7	3.9	5.2	18.0
	%	5.6%	5.0%	3.8%	2.6%	2.2%	3.1%	2.8%	1.8%	1.1%	1.4%	3.8%
Inter Segments	**Sales**	-1.2	-1.7	-1.9	-3.2	-3.5	-3.4	-3.3	-2.3	-1.7	-2.2	1.7-
	%	-1.5%	-1.7%	-1.4%	-1.6%	-1.6%	-1.3%	-0.9%	-0.7%	-0.5%	-0.6%	0.4%-
Total Sales		84.0	102.9	139.8	191.2	214.6	260.0	374.6	316.7	338.7	386.9	473.1

The following is a summary of the profit and loss reports for the first nine months of 2011 - 2012 (US$ M):

During the first nine months of 2012 Frutarom achieved record highs in sales and in gross, operating and net profits, EBITDA and earnings per share, despite the strengthening of the dollar versus the main currencies in which it operates (European currencies and the NIS), which detracted from sales and profits in dollar terms.

	2011	2012	Change (%)
Sales	386.9	473.1	22.3%
Gross profit	141.8	174.8	23.2%
R&D, selling, Administration, General and Other expenses	95.3	115.6	21.3%
Operating profit	46.5	59.1	27.1%
EBITDA	62.3	79.8	28.1%
Financing expenses	2.6	5.8	127.3%
Pretax profit	44.0	53.3	21.3%
Net profit	34.1	41.4	21.5%

Gross Profit

The Company's gross profit for the first nine months of 2012 increased by 23.2%, reaching a record high for the first nine months of US$174.8 M compared with US$141.8 M for the first nine months of 2011. Gross margin net of Trade and Marketing activity added following the acquisition of Etol (a non-core activity of Frutarom), reached 37.9% compared with gross margin of 36.7% during the same period in 2011. Gross margin including Etol's Trade and Marketing activity added following the acquisition of Etol also increased, reaching 36.9%.

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

In the first nine months of 2012 selling, marketing, research and development, general and administrative and other expenses totaled US$115.6 M (24.4% of sales) compared with US$95.3 M (24.6% of sales) in the first nine months of 2011.

The selling, marketing, research and development, general and administrative and other expenses included one-time reorganization expenses in the amount of US$1.0 M. Other income included net one time income of US$0.8 M (negative goodwill for the acquisition of Etol in the amount of US$1.7M, set off by one–time acquisition expenses in the amount of US$0.9 M), thus the net impact on operational profit was one-time expenses of US$0.2 M.
During the same period last year, selling, marketing, research and development, general and administrative and other expenses included one-time expenses for acquisitions in the amount of US$1.6 M.

The increase in expenses was mainly due to the increase in the scope of activity, and mainly from acquisitions performed over 2011 and Q1 2012.

Frutarom constantly acts to achieve maximum efficiency, improve its cost structure and strengthen its future competitiveness, while maximally utilizing its manufacturing sites throughout the world and successfully integrating its latest acquisitions.

Operating Profit and EBITDA

In the first nine months of 2012, operating profit increased by 27.1% reaching a first nine month high of US$59.1 M (12.5% of sales) compared with US$46.5 M (12.0% of sales) over the same period last year.

The EBITDA achieved by Frutarom in the first nine months of 2012 increased by 28.1% reaching a first nine month record high of US$79.8 M (16.9% of sales), compared with US$62.3 M (16.1% of sales) in the same period last year.

Finance Expenses

Over the first nine months of 2012, finance expenses totaled US$5.8 M (1.2% of sales) compared with finance expenses of US$ 2.6 M in the first nine months of 2011 (0.7% of sales).

Interest expenses in the first nine months of 2012 totaled US$5.6 M compared with US$1.2 M during the same period last year. The increase in interest expenses derived from an increase in the loan balance, due to the acquisitions performed.

Finance expenses due to currency exchange rate differentials totaled US$0.3 M compared with US$1.4 M over the corresponding period last year.

Pretax profit

In the first nine months of 2012, pretax profit increased by 21.3%, achieving a first nine month record high of US$53.3 M (11.3% of sales) compared with US$44.0 M (11.4% of sales) in the first nine months of 2011.

Taxes on Income

In the first nine months of 2012, taxes on income totaled US$11.9 M (22.3% of pretax profit) compared with US$9.8 M (22.4% of pretax profit) in the first nine months of 2011. The tax rate during the first nine months of 2011 was affected mainly by income from taxes for previous years in the amount of US$1.0 M (net of such aforesaid tax income, the tax rate for the first nine months of 2011 stood at 24.7%).

Net Profit

In the first nine months of 2012 net profit increased by 21.5%, reaching a first nine months high of US$41.4 M compared with US$34.1 M in the first nine months of 2011. Net margin amounted to 8.8% similar to the first nine months of 2011.

Earnings per Share

In the first nine months of 2012, earnings per share reached a record of US$0.72 per share compared with US$ 0.59 per share in the first nine months of 2011.

E. LIQUIDITY

Q3 2012 again showed a marked improvement in the Company's cash flow from operating activities, reaching US$22.7 M, compared with a cash flow of US$16.6 M for the same quarter last year.

Over the first nine months of 2012 cash flow from operating activities increased by 93% reaching US$62.6 M, compared with US$32.5 M during the corresponding period last year.

The increase in cash flow from operating activities over the first nine months derived mainly from the growth in profit and the actions taken for optimizing inventory levels.

Frutarom continuously acts to maintain an optimal level of working capital suited to the expected growth rate, taking into account seasonality, supply of the various raw materials and their current and future anticipated prices.

F. SOURCES OF FINANCE

Sources of Equity

Frutarom's equity as at September 30, 2012 totaled US$434.7 M (56.6% of the total balance sheet) compared with US$395.5 M (64.6% of its total balance sheet) as at September 30, 2011 and US$393.6 M as at December 31, 2011 (60.6% of its total balance sheet). The change derives mainly from the growth in net profit during the period, offset by a reduction in capital reserve from translation differentials in light of the strengthening of the dollar versus European currencies and the NIS (not including the Pound Sterling) as of September 30, 2012 compared with September 30, 2011.

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

Average long-term credit from banks provided to the Company in Q3 2012 totaled US$186.3 M compared with US$46.90 M in Q3 2011. The increase is a result of increased loan balance for financing the Company’s acquisitions.

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

Average short -term credit from banks provided to the Company in Q3 2012 totaled US$12.3 M compared with US$57.3 M in Q3 2011. The reduction is a result of the replacement of short term loans which the Company took for interim financing of acquisitions with long term loans.

Supplier and Customer Credit (Average)

In Q3 2012, the Company utilized supplier and other credit in the amount of US$93 M compared with US$68.0 M in the same quarter last year. During Q3 2012, the Company granted US$116.0 M credit to its customers, compared with US$88.6 M during the same period last year. The increase in supplier and customer credit is mainly the result of the increase in the Group's sales and its activities, and of its recent acquisitions.

EXPOSURE TO MARKET RISKS AND THEIR MANAGEMENT

During Q3 2012 there were no substantial changes regarding the Company's exposure to market risks and its management of such, including the impact of the Company's indexation balance compared to the Company's report on this matter in its periodic report for 2011 published by the Company on March 15, 2012, apart from the loan balance, which increased as a result of the Company’s latest acquisitions. As of September 30, 2012 the Group has a long term loan after deduction of current maturities in a total amount of US$142.8 M, and its short term loans, including current maturities of long term loans, total US$53.6 M. The Company has cash balances of US$44.3 M.

SENSITIVITY TESTS

Sensitivity to Changes in the US Dollar- NIS Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	**+10%**	**+5%**	**-**	**-5%**	**-10%**
Exchange rate	**4.303**	**4.108**	**3.912**	**3.716**	**3.521**
Cash and cash equivalents	(62)	(31)	621	31	62
Customers	(1,040)	(520)	10,401	520	1,040
Other debtors	(38)	(19)	378	19	38
	(1,140)	**(570)**	**11,400**	**570**	**1,140**
Bank loans	754	377	7,541	(377)	(754)
Suppliers and service providers	356	178	3,563	(178)	(356)
Other creditors	-	-	-	-	-
	1,110	**555**	**11,104**	**(555)**	**(1,110)**
Total exposure, net	**(30)**	(15)	**296**	**15**	**30**

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	**0.678**	**0.647**	**0.617**	**0.586**	**0.555**
Cash and cash equivalents	(351)	(176)	3,514	176	351
Customers	(1,269)	(634)	12,688	634	1,269
Other debtors	(113)	(57)	1,132	57	113
	(1,733)	**(867)**	**17,334**	**867**	**1,733**
Bank loans	2,593	1,296	25,929	(1,296)	(2,593)
Suppliers and service providers	637	319	6,370	(319)	(637)
Other creditors	958	479	9,578	(479)	(958)
Other long term creditors	38	19	381	(19)	(38)
	4,226	**2,113**	**42,258**	**(2,113)**	**(4,226)**
Total exposure, net	**2,493**	**1,246**	**(24,924)**	**(1,246)**	**(2,493)**

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	**0.850**	**0.811**	**0.772**	**0.734**	**0.695**
			US$ 000		
Cash and cash equivalents	(1,515)	(758)	15,154	758	1,515
Customers	(4,786)	(2,393)	47,862	2,393	4,786
Other debtors	(191)	(96)	1,912	96	191
	(6,492)	**(3,247)**	**64,928**	**3,247**	**6,492**
Credit from banks	10,122	5,061	101,219	(5,061)	(10,122)
Suppliers and service providers	2,158	1,079	21,584	(1,079)	(2,158)
Other creditors	1,105	553	11,051	(553)	(1,105)
	13,385	**6,693**	**133,854**	**(6,693)**	**(13,385)**
Total exposure, net	**6,893**	**3,446**	**(68,926)**	**(3,446)**	**(6,893)**

Sensitivity to Changes in the US Dollar-Swiss Franc Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	**+10%**	**+5%**	**-**	**-5%**	**-10%**
Exchange rate	**1.028**	**0.981**	**0.934**	**0.888**	**0.841**
Cash and cash equivalents	(208)	(104)	2,082	104	208
Customers	(783)	(391)	7,828	391	783
Other debtors	(56)	(28)	556	28	56
	(1,047)	**(523)**	10,466	**523**	**1,047**
Suppliers and service providers	388	194	3,882	(194)	(388)
Other creditors	758	379	7,575	(379)	(758)
	1,146	**573**	**11,457**	**(573)**	**(1,146)**
Total exposure, net	99	**50**	**(991)**	**(50)**	**(99)**

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	(957)	(479)	9,571	479	957
Customers	(1,523)	(762)	15,233	762	1,523
Other debtors	(63)	(31)	625	31	63
	(2,543)	**(1,272)**	**25,429**	**1,272**	**2,543**
Credit from banks	163	82	1,634	(82)	(163)
Suppliers and service providers	206	103	2,056	(103)	(206)
Other creditors	244	122	2,440	(122)	(244)
Other long term creditors	69	35	693	(35)	(69)
	682	**342**	**6,823**	**(342)**	**(682)**
Total exposure, net	**(1,861)**	**(930)**	**18,606**	**930**	**1,861**

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 (RMB)	15	8	1,618	(8)	(16)
Total exposure, net	**15**	**8**	**1,618**	**(8)**	**(16)**

G. SUMMARY OF SENSITIVITY TESTS TABLES

The functional currency of the majority of the Group's companies is the local currency in their respective countries of residence; therefore, the translation differences of these companies' balance sheet balances do not affect the Company's profit and loss report and are directly attributed to the Company's equity (currency translation capital fund).

Sensitivity to Changes in the US Dollar- NIS Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	+10%	+5%	-	-5%	-10%
Exchange rate	4.303	4.108	3.912	3.716	3.521
	US$ 000				
Total Exposure, net	(30)	(15)	296	15	30

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	0.678	0.647	0.617	0.586	0.555
	US$ 000				
Total Exposure net	2,493	1,246	(24,924)	(1,246)	(2,493)

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	0.850	0.811	0.772	0.734	0.695
	US$ 000				
Total exposure, net	6,893	3,446	(68,926)	(3,446)	(6,893)

Sensitivity to Changes in the US Dollar-Swiss Franc Exchange Rate

	Profit (Loss) from changes		Fair value	Profit (Loss) from changes	
% of change	+10%	+5%	-	-5%	-10%
Exchange rate	1.028	0.981	0.934	0.888	0.841
	US$ 000				
Total exposure, net	99	50	(991)	(50)	(99)

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	(1,861)	(930)	18,606	930	1,861

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	15	8	1,618	(8)	(16)

CORPORATE GOVERNANCE ASPECTS

APPROVAL PROCESS OF THE FINANCIAL STATEMENTS

The Company's financial statements are submitted for approval to the Board of Directors, the body responsible for the Company's governance, a few days after the Board of Directors' committee for the review of the financial statements (the "**Balance Sheet Committee**") discusses the financial statements and forms its recommendations to the Board of Directors in accordance with the Companies Regulations (Instructions and Terms for the Approval Procedure of the Financial Statements), 2010 ("**Statements Approval Regulations**").

Members of the Company's Board of Directors

The Company's Board of Directors is comprised of seven members, five of whom are directors with accounting and financial expertise as detailed below. For further details regarding the Company's directors see regulation 26 to Chapter D of the Company's periodic report for 2011, published on March 15, 2012 (Further Details on the Corporation).

Balance Sheet Committee and Members

The members of the Balance Sheet Committee are the members of the Audit Committee – Ya'acov Elinav, External Director and chairman of the committee, Isaac Angel, External Director, and Gil Leidner, Director. The Balance Sheet Committee members have financial and accounting expertise and the capacity to read and understand financial statements, and have provided the Company with a written declaration in this regard. Mr. Ya'acov Elinav and Mr. Isaac Angel are independent directors by virtue of their being external directors. Mr. Gil Leidner is an independent director in accordance with the determination of the Company's Audit Committee of May 19, 2011, and the determinations of the Board of Directors on August 17, 2011. For details regarding the skills, education and experience of the members of the Balance Sheet Committee, based on which the Company refers to them as directors with financial and accounting expertise, see regulation 26 in Chapter D of the Company's periodic report dated for 2011, published on March 15, 2012 (Further Details on the Corporation).

Balance Sheet Committee Processes for Forming Recommendation to the Board of Directors

The Company's financial statements were discussed at the meeting of the Balance Sheet Committee held on November 22, 2012. The members of the committee received the financial statements several days prior to the meeting. The 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. Karin Ben Ari, a legal counsel in the Company. At the meeting, presentations were given by the Company and by the auditors. The Balance Sheet Committee discussed, among other things, the estimates and evaluations included in the financial statements, the internal control on financial reporting, the completeness and fairness of the disclosure in the financial statements, the accounting policy adopted and the financial practice implemented with regard to the material matters of the Group, and the valuations, including the assumptions and estimations on which the data in the financial statements is based. Within the discussion, the Balance Sheet Committee formed its recommendations to the Board of Directors in accordance with the Statements Approval Regulations. The recommendations of the committee were delivered to the Company's Board of Directors two business days prior to the Board meeting at which the financial statements were discussed, which in the opinion of the Board of Directors and in accordance with its resolution was a reasonable time period in light of the scope and complexity of the recommendations.

Approval Procedure of the Reports by the Board of Directors

The members of the Board of Directors received the draft of the financial statements several days prior to the date of the Board meeting at which the statements were submitted for their approval. The Company's independent auditors and members of the Company's senior management were 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 Global Supply Chain and Operations, Mr. Guy Gill - Vice President of Finance, and Ms. Tali Mirsky - Global Vice President of Legal Affairs and Corporate Secretary. The Company's internal auditor, Mr. Yoav Barak, was also invited to that meeting. During the meeting, the Board of Directors discussed the recommendations of the Balance Sheet Committee regarding the financial statements, and the President and CEO and Executive Vice President and CFO presented the Group's business and financial results for the relevant period in comparison with previous periods, emphasizing special events that occurred during the period, to the Board of Directors. During the presentation of the results of the Group, the Company's management members answer questions and relating to the Directors' comments. Following presentation of the Company's financial results, the Company's independent auditors answered the Directors' questions. Finally, the Board of Directors votes on approval of the financial statements. All of the members of the Board of Directors were present at the Board meeting held on November 26, 2012, where the financial statements for September 30, 2012 were unanimously approved.

Amendment of the Company's articles of association and indemnification of Officeholders

On June 10, 2012 the Company's General Meeting approved, inter alia, the amendment of the Company's articles of association in a manner adapting them to the updated version of the Companies Law and of the Efficiency of Enforcement Proceeding of the Securities Authority (Legislation Amendments) Law, 2011 ("**Administrative Enforcement Law**"), updating undertakings for indemnification of officeholders and directors who are not controlling members or their relatives, granting approval of undertakings for indemnification of directors who are controlling members or their relatives for a period of three years, expansion of the existing insurance policy for directors and officeholders who are not controlling shareholder or relatives of such in a manner which will include events which may be insured under the Administrative Enforcement Law and increase the limit of liability of the insurance and engagement under the directors' insurance policy for directors who are controlling members or their relatives under conditions identical to those given to directors who are not controlling members or their relatives for a period of three years.

For more details see the supplementary report on the convening of a general meeting of the Company published by the Company on March 15, 2012 and the immediate report on the results of the general meeting published by the Company on June 11, 2012.
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DISCLOSURE RELATING TO THE CORPORATE FINANCIAL REPORTING

A. DIVIDEND DISTRIBUTION IN 2012

On March 14, 2012, the Company's Board of Directors resolved to approve a distribution of cash dividend in the amount of NIS 0.2 per share. The dividend, in the total amount of US$3,029 thousand, was paid on May 6, 2012.

B. LOAN AGREEMENT

On June 25, 2012 the Company, through its subsidiary Frutarom Switzerland Ltd., signed an agreement for a loan of €50.0 M from two banking corporations in Switzerland. The loan was taken for financing 100% of the share capital of Etol, and replaced the short term loan the Company had taken for interim financing, and also served to repay part of the loan Etol had taken from banking corporations in Slovenia.

For further details regarding the loan see the Company's immediate report on the matter dated June 26, 2012.

C. CRITICAL ACCOUNTING ESTIMATIONS

No significant change has occurred in the report period compared with the Company's periodic report for 2011, published on March 15, 2012.

D. EXCLUSION OF THE COMPANY'S SEPARATE FINANCIAL STATEMENTS UNDER REGULATION 9(C) TO THE REGULATIONS

The Company did not include in its Periodic Report a separate financial statement as set forth in Regulation 9C to the Regulations (the **"Solo Statement"**) , due to the negligibility of the additional information of such statements and the fact that a Solo Statement would not add any material information for a reasonable investor, not included in the Company's consolidated statements.

The Company determined that the information is negligible as the Company does not have any commercial activities of any kind whatsoever and therefore the Company's results of operations have no effect on the Groups' consolidated profit and loss statements. The Company does not employ people and it does not have any sales or expenses toward third parties.

All of the Company's revenues (dividend and financing income on re-evaluations of capital bills versus Frutarom Ltd.) derive from Frutarom Ltd.

From a balance sheet aspect, other than the settling of accounts with the income tax authority, the Company has no balances versus third parties. The only balances it has are loans and balances to Group members (fully owned) and land in the amount of US$139 thousand.

The management of the Company has determined that so long as income from externals or from companies not fully held by the Company are lower than 5% of total revenues in the consolidated financial reports, and so long as expenses to externals or companies not fully held by the Company are lower than 5% of total expenses in the consolidated financial statements, the Company's separate financial information under regulation 9C to the Regulations is negligible, and the absence of such does not affect investors' ability to estimate the Company's liquidity risks and does not add any substantial information for reasonable investors.

The management of the Company has also examined the warning signs contained in Regulation 10(14) to the Regulations and determined that they do not exist.

The Board of Directors held one meeting over Q3 2012.

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

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

November 26, 2012