



Manufacturers Association of Israel The Energy Committee

February 23, 2009

To:
Mr. Jonathan Shtibel
ICL Inc.

RE: The status of natural gas use in Israeli industry

The Manufacturers Association of Israel (MAI) is the sole representative body of all industrial sectors in Israel, including private, public, and government industries. With more than 2000 direct or affiliate members MAI is a leading economic force in Israel.

In recent years, following the discovery of natural gas reserves off the coast of Ashkelon, the Israeli government has sought to build both the infrastructure and regulatory framework that would enable widespread industrial use of natural gas as a fuel source. Given the clear environmental benefits, MAI views with great importance any effort to encourage industry to switch to natural gas.

Unfortunately, natural gas cannot yet be seen as a secure source of fuel for Israeli industry beyond the short term. Israel's proven reserves are far too small to meet forecasted demand, which is expected to be 9 BCM annually beginning in 2015. For the time being, Israeli industry remains dependant on imported Egyptian gas as the sole potential source of long-term supply. However, there continue to be disruptions in this supply, which began in May 2008. This poses a significant risk for industry, as this sole supply of natural gas is extremely sensitive to geopolitical tensions in the region. In an attempt to secure an additional supply of natural gas, drilling is underway at a few potential sites along Israel's coast. An additional reserve was discovered 90 km off the coast of Haifa in January 2009, and further tests are required in order to determine its exact size. Israel is also exploring the feasibility of liquefied natural gas (LNG), and has taken initial steps towards the construction of a facility that can receive LNG. Neither of these projects will be able to supply the Israeli market with natural gas prior to 2015.

At this stage Israeli industry remains uncomfortable with the national transmission system as well, amid concerns that both the national pipeline and the international pipeline from Egypt do not have the capacity to meet updated demand forecasts. The radius of significant sections of the pipeline is too small; in order to meet the new demand forecasts, the pipeline along this section must be doubled. Otherwise, the limited capacity of the transmission system will leave at least some private industrial users without access to natural gas.

Delays in the pipeline construction have placed additional risks on those few facilities that have pursued a conversion to natural gas in recent years. For instance, while the first section of the national pipeline was expected to be completed by the end of 2006, not until mid-2008 was the connection to the IEC's Gezer power plant in place. Similarly, the connection of southern factories such as Rotem Amfert Negev, Bromine Compounds, Dead Sea Works, Dead Sea Magnesium, and Bromine Compounds – Periclase site to the transmission system is not expected to be completed until mid-2009, more than a year and a half later than planned. This segment may be subject to yet further delays. Those isolated few companies that have invested in a conversion to natural gas in recent years have thus done so in a

period of extreme uncertainty regarding both the timing and extent of the availability of the gas.

There have been several reasons for the delays in the pipeline. The main reason has been problems with acquiring the necessary statutory permits and authorizations. Due to the lack of experience in Israel with natural gas, a dangerous substance that requires strict safety and operational precautions, the state required that the national transmission system be approved by a wide range of entities.

The construction was also delayed due to the late delivery of several major types of equipment, including Pressure Reducing and Metering Stations (PRMS) and valves, as well as delays on the part of project subcontractors due to financial disputes.

Due to extensive legislation in recent years, including the Natural Gas Sector Law of 2002, the Building and Planning Regulations (Low Pressure Natural Gas Facilities) 2006, the Natural Gas Market Regulations (Work Plan for Distribution Network) 2006, any private company converting to natural gas must take a number of steps that require a significant investment of both time and capital.

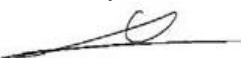
For instance, industrial users must contract foreign companies to both approve the infrastructure plans and install the natural gas equipment, as well as to implement new safety systems. Industrial users must also implement training programs for all employees expected to work with the natural gas. This is necessitated due to the additional safety hazards posed by the use of natural gas and the fact that Israeli industry is inexperienced in this field.

As a result of these obstacles, the vast majority of industrial companies are unwilling at this stage to commit to a conversion to natural gas, and are instead waiting for a significant portion of the uncertainty to be eliminated. In fact, to date the only industrial company to convert to natural gas without government ownership or a government safety net is the American Israel Paper Mills (AIPM), which began consuming natural gas in 2007. In switching to natural gas, AIPM took advantage of the additional revenues provided by the Clean Development Mechanism (CDM). These additional revenues played a decisive role in justifying the risks faced by AIPM in converting to natural gas.

In addition to AIPM, three other companies currently consume natural gas in Israel. The Israel Electric Corporation, Israel's national electricity company, is government-owned and has used natural gas since the end of 2004. Ashdod Refineries converted in 2005 while still a government-owned company. The IPP Delek Ashkelon plant was constructed following a government tender in order to supply electricity to Israel's sole desalination plant, a strategic piece of infrastructure, and therefore the government encouraged its construction by providing it with a safety net.

Despite the above obstacles, in light of its environmental benefits MAI continues to view the use of natural gas as a strategic objective for Israeli industry, and as such encourages any initiative that can accelerate the spread of this technology in Israel. CDM, and the additional revenues it provides, can help Israeli industry overcome the numerous obstacles to natural gas use that it continues to face.

Sincerely,



Oren Harambam
Director

The Energy Committee, Manufacturers Association of Israel