

## Israel Hi-Tech Investment

'Though 2014 was a hallmark year for Israeli startups, we are far from reaching the industry's full potential.' Chief Scientist Avi Hasson.

High-tech is one of Israel's most robust areas of the economy today, but the report warns that while the startup sector is strong, and new companies continue to sprout, too many are making quick exits, rather than growing into mature companies.

The growth of mature domestic companies is crucial to Israel's economy, the report says, because large companies employ a higher number and wider variety of employees, and also help develop know-how within Israel.

As such, it recommends creating incentives and conditions that will make it worthwhile for Israeli companies to continue their growth in Israel. More companies like Outbrain or ironSource are needed for Israel to become a market leader, says the report.

Aside from efforts to turn more startups into mature companies, the recently released first edition of the report identifies three other areas Israel must address to keep the tech sector strong – new funding, the development of new technologies in traditional industry and the public sector, and smarter and more efficient government involvement.

As for foreign funding, the report notes a growth in foreign investors in Israeli tech companies. In 2013, foreign investors funded 75% of investments in Israeli companies and 85% of all capital raised by Israeli VCs.

According to the report, foreign funding is responsible for up to about half the R&D funding in Israel. Most foreign funding invested in Israeli VCs comes from the United States, but in the last three years, there has been increasing interest from investors in Asia, mainly from China.

"The ecosystem in which the high-tech industry operates is multifaceted and complex. We identified five core components in this ecosystem: innovation policy, human capital, funding, industrial innovation and international activity," said Hasson.

"The report raises issues affecting anyone concerned with advancing the high-tech industry and implementing innovation in the private and public sectors. Reviewing these issues is meant to serve as a basis for ongoing dialogue between the industry, investors, entrepreneurs and the government, and to direct our joint efforts towards attaining economic prosperity through technological innovation." <sup>1</sup>

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<sup>1</sup> <http://www.israel21c.org/the-best-is-yet-to-come-for-israeli-high-tech/>

Growth of the Israeli economy has been largely fueled by a steady increase in exports and by skyrocketing international investment. Foreign direct investment (FDI) in Israel reached \$4.4 billion in 2009. By 2011, it had reached a high of \$10.8 billion, while in 2013, total foreign investment totaled \$11.8 billion (Source: Central Bureau of Statistics). Public Debt as a percentage of GDP has steadily declined from 102% in 2003 to 4.7% in 2007 to 69.8% in 2011 to a record low 67.%, in 2013, while unemployment has continued to decline and stood at 5.8% as of Q1/2014 (Source: Ministry of Finance). In 2013, 32.6% of Israel's GDP was exported in the form of goods and services (\$95.1 billion). (Source: Israel Ministry of Finance)

IMD Global Competitiveness Yearbook 2013 ranked Israel 1st in the world for its central bank policy -- the fourth year in a row that it leads in the top five -- and 4th for the resilience of its economy, while WEF Global Competitiveness Yearbook 2014-2015 ranks it 1st for annual percentage change of inflation and 6th for investor protection out of 148 economies.

Sound macroeconomic strategy, coupled with the relatively conservative approach driving the Israeli banking sector's strategic decisions, has fueled Israel's strong economic performance, even as the global economy has contended with crippling economic slowdown. In fact, since 2004, Israel's growth rate has exceeded the average growth rate of all advanced economies. In 2009, as most of the world experienced a decline in GDP, Israel experienced a 1.1% growth in its GDP. Its real GDP growth rate in 2013 was 3.3%, while as of Q1/2014 it stood at 2.9% (Source: Israeli Ministry of Finance).

From its inception, Israel has utilized its ingenuity to forge bold and pioneering solutions to global challenges. Israeli ingenuity and its innovation ecosystem enable Israeli companies to bring product ideas to market quickly and efficiently, acting as a pipeline of pioneering technologies to the world across a range of vital sectors like cleantech, agriculture, cyber security and digital media.

### Agriculture

Within today's daunting challenges of an exploding world population – projected to reach 9 billion by 2050 -- coupled with dwindling resources, the imperative to find creative ways to increase food production while reducing input is paramount.

Through new technologies, Israeli companies are helping to find ways to increase crop yield, resist climate change and reduce resource consumption.

Amongst a range of Israel inventions designed to promote long-term sustainability, satellite imagery, information technology, and geospatial tools help farmers across the globe track harvests and manage resources.

Israeli technologies are widely sought after in both the industrial and developing worlds. For example, each year, Israel exports over \$150 million worth of seeds, mainly hybrid vegetable seeds, to markets that depend on improved yields and quality. (Source: Israeli Ministry of Agriculture)

### Cyber Security

In a climate of growing global awareness of the risks of privacy breaches on the World Wide Web, the world is increasingly relying on Israel's expertise to ward off computer threats and keep information secure.

Combining exceptional hi-tech capabilities with skills honed over decades contending with the threats of terrorism, Israel has emerged as a world leader in cyber security, ranked 1st by IMD 2013. The flow of information between Israel's military, industry, and academia mean the best of research and inventiveness find their way to market, helping to protect the central engine of the modern economy, the Internet.

Defining cyber security as a national priority, the Israeli government has further established the National Cyber Bureau, which is engaged in targeted efforts to secure the cyber front. The Bureau coordinates efforts between the military, education, and business sectors to guarantee computer and Internet safety, with major implications for the economy at large.

In the cyber domain, Israeli specialists offer a wide range of cyber security solutions, including telecommunication and network security technologies, financial processing and data security technologies, and communications surveillance.

In 2014, over 220 local companies alongside 20 foreign R&D centers develop security solutions applied throughout the world including:Paypal, IBM, EMC, RSA, GE, VMWare, General Electric, Cisco, Deutsche Telekom, Lockheed Martin, CA Technologies, McAfee. IBM, Cisco, and GE are establishing major cyber centers in Israel, recruiting hundreds of local employees in the process.

In the past 4 years alone, over 100 new cyber-security companies have sprouted up in Israel, with nearly \$400 million invested in 78 companies during this period. (Source: IVC Research Center)

### Health & Science Technologies

Soaring global health care costs, an increasingly aging population, and emerging middle classes in the developing world, demand that the healthcare industry respond with urgency and creativity.

Israel's over 1,000 life and health science companies, which lead the world in medical device patenting per capita, are responsible for producing a range of innovations, paving the way toward personalized medicine in the future.

In the Medical Devices arena, Israeli scientists and engineers have integrated advanced technologies in Electronics, Communications and Electro-optics to develop world-class innovations in digital imaging, medical lasers, tele-medicine, as well as diagnostic and surgical equipment. Israel has further been the source of breakthrough treatments and blockbuster drugs, generating billions of dollars in annual sales, including Copaxone for the treatment of MS and Rebif for the treatment of Central Nervous System Disorders.

In 2013 alone, Israel exported \$6.3 billion in pharmaceutical products, accounting for almost 10% of the country's total exports.

### New Media& Internet Sector

Emerging from within an entrepreneurial culture that pursues rapid results and quick, smart technological solutions to common problems, Israeli new media companies are vital players in an increasingly digital world.

Drawing on the country's traditional areas of expertise, IT and Telecom, Israel's 700+ new media companies apply the best of creativity and adaptability to the full spectrum of new media fields.

Israeli companies span the range of new media possibilities, including: content creation, big data, storage, delivery and management, gaming, broadcast, digital & cable TV, interactive TV, IPTV and satellite services, online advertising, e-commerce, optimization, analytics, and user interface solutions.

Exporting more than \$2 billion annually, Israeli companies are sought after by media outlets, operators, and content providers for their novelty and utility, which create a rich user experience while increasing revenue.

### Water Sector

Israel's water industry is anchored in a long history of creativity and resourcefulness, overcoming the challenges of an arid climate being vital to Israel's growth since its establishment. Driven by circumstance to maximize its creative capacity, Israel's innovations in the realm of water technologies, water management and long-term planning have made sustainable water consumption a reality in 2014, and well into the future.

Among the impressive range of Israeli innovations, nation-wide reclamation of treated domestic wastewater for irrigation in the agricultural sector, solutions for industrial wastewater and desalination have been especially ground-breaking.

- 86% of Israel's wastewater is reclaimed for agriculture, which is by far the highest percentage in the world.

- Worldwide, Israeli companies have installed more than 350 desalination plants in nearly 40 countries.

- Israel is among the world's lowest-cost producers of desalinated water: \$0.55 per cubic meter, compared with \$1.00 per cubic meter, which is the world average.

- Between 2005 & 2010 alone, Israeli water-related exports doubled. Today, Israeli systems account for some 50% of the low-pressure irrigation systems on the global market, Israel exporting more than 80% of its drip irrigation products, which reduce agricultural water consumption by one-third. Source: The Israel Water Authority and The Israel Export Institute

### Hi-Tech Capital

2013 was a record-breaking year in terms of the amount of capital raised in the hi-tech industry, with a whopping 662 Israeli high-tech companies closing financing rounds. \$2.3 billion worth of capital was raised, a 13-year high.

The final quarter of 2013, in particular, saw soaring capital investment, with more deals completed and in greater volume than any quarter since the year 2000. 191 Israeli high-tech companies raised \$751 million during that period, including 110 VC-backed deals that attracted a total of \$554 million.

In total, 2013 saw 395 VC-backed hi-tech capital deals, which attracted \$1.7 billion in funding – 74% of the total. The average financing round of VC-backed deals reached \$4.3 million.

Foreign investors have considerably increased their investments in Israeli high-tech and account for a vast majority – 76% -- of capital investment in Israeli companies.

Israeli High-Tech Capital Raised 2013-2014 (\$M)

The majority of investments over 2013 – two-thirds – was follow-up investment, with first-time investments constituting only one-third of the total.

The life-science sector led funding rounds in 2013, attracting 23% of total funds raised, or \$522 million. Trailing just behind it was the software sector, which raised 21% of total capital. Both cyber security and data reached peak investment levels, as did cloud infrastructure and big data. Source: IVC Research Center and KPGM.

<http://www.forbes.com/sites/rogeraitken/2015/05/15/israeli-tech-investing-could-the-best-opportunities-yet-be-ahead/2/>

Commenting in the first annual Innovation Report on Israel's high-tech sector, which was introduced by the Office of the Chief Scientist (OCS) on 15 April 2015, Mr Hasson noted: "Our challenge in the coming years will be to remain at the forefront of global technology while implementing innovative measures in all aspects of the market and economy."

That said, the report which presents an overview of the Israeli hi-tech industry while outlining the trends, challenges and opportunities, identifies four "significant measures" that should be undertaken to meet the challenges.

The measures include creating new sources of funding for the industry, turning more hi-tech companies into major companies, implementing and developing technologies in traditional industries and in the public sector, as well as having smarter government involvement. So, despite much progress there appears no time to rest on their laurels.

It is envisaged that the report will "stimulate on-going dialogue between industry, investors, entrepreneurs and the government to direct our joint efforts towards attaining economic prosperity through technological innovation."

Simon Tobelem, Founding Partner of Arie Ventures, a UK-based venture capital (VC) firm focused on investing in Israeli technologies and that launched two new funds in late March to invest in Israeli tech (in conjunction with Taurus Asset Finance), remarking on the current "boom" in the sector says one has to look at the "bigger picture" than just the Israeli market.

This is for two reasons. Israeli companies are a third by number of the IPOs on Nasdaq, after China and the US. London-based Tobelem commenting says: "A huge amount of the value created is not in Israel. Therefore, most of the impact of successful Israeli start-ups is felt in US IPOs and large M&A deals driven mostly by US, and more recently Chinese investors."

He adds that there is "no question the market continues to grow." The figures would seem to speak for themselves. For instance, in 2013 and 2014 there were fourteen exits (IPO/M&A deals) above \$300m, which represents an "overwhelming increase" in activity given that between 2003 and 2012 when there were just twelve. Furthermore, over 1,000 start-ups were created each year (in the country) in 2013 and 2014. And, to cap that off the number of venture deals stands at 600-700 per year.

Other sectors of the Israeli economy are also performing robustly. Israel is a leader in agri-tech business, water treatment and irrigation solutions as well as chemicals and plastics, diamond-cutting and military industries. The Israeli banking system has also performed pretty well too and displayed what Tobelem describes as "outstanding stability" during the whole of the financial crisis.

A new report by the the Israel Venture Capital (IVC) Research Center shows that Israel's tech economy is attracting more investment money than ever – as well as a better "class" of investor.

The report issued Tuesday found that Israeli high-tech firms set a new record for financing in the second quarter of 2015 – breaking the record set in the last quarter of 2014. The report said that 179 Israeli high-tech firms raised a total of \$1.12 billion during Q2/2015 – beating the \$1.11 billion raised in Q4 2014.

The IVC report also shows that Israel is attracting more attention from private equity investors, a development that portends well for the tech economy, according to Koby Simana, CEO of IVC Research Center. “If we want the local high-tech industry to continue growing and see more large-scale, mature companies emerge, there is room for technology investments from more than just venture capital funds, local or foreign,” said Simana. “The industry needs a variety of investors and investment models to support companies throughout various stages.”

Much of the Q2 investment money came from foreign private equity (PE) investors, the IVC data show – with venture capital-backed (VC) investments hitting a six-year low. That change, said Simana, is a sign of maturity for the Israeli tech economy; while VCs generally invest in earlier growth-stage companies and start-ups, PE investors seek out companies that are more mature, with bigger sales and larger markets, further along on the road to “making it big.”

Many of those PE investors apparently are coming from Asia, another positive development for the Israeli tech economy, which is now a “world brand,” as opposed to a specialized market that appealed to VCs looking for “bargains” in companies with promising early-stage technology.

“Investors from Asia are investing in an increasing number of Israeli growth companies, adding to the overall amount of cash available for market expansion,” said investment expert Ofer Sela, a partner at KPMG Somekh Chaikin’s Technology group.

“Overall, Israeli portfolio companies are priced much more reasonably than Silicon Valley companies, making Israel an attractive location for both investments and acquisitions,” said Sela. The trends “reflect the health of the venture-backed ecosystem in Israel and the patience of investors supporting their portfolio companies that can grow into ‘unicorns,’ tech companies that become world-class organizations, that are substantial and mature.”

Besides netting more money as an aggregate, individual companies in the Israeli tech industry – which encompasses companies in systems, networking, biotech, mobile tech, environmental technology, and other areas – also netted more money on average individually. In the first half of 2015, the average financing round for tech firms was \$6.2 million, compared to \$4.8 million in the first half of 2014, and \$2.9 million in that same six-month period in 2013.

Even more important, said Sela, was that many more tech firms had raised significantly more than the average. “Fifty percent of the amount raised during this quarter, and even more since the beginning of 2015, results from large deals of \$20 million or more raised per round,” said Sela. “The overall number of growth companies attracting investments continues to increase quarter over quarter.”

The software industry led fundraising in Q2/2015, for the first time since Q1/2013, with \$487 million (44% of total money raised) invested in 50 companies. The amount was the largest ever for the sector, almost triple the last two-years’ average. Internet and life science investments, which led all sectors in Q1/2015, decreased reaching 21% and 13% respectively.

In Q2/2015, late stage companies accounted for the majority of investments, with \$480 million, followed by mid-stage companies with \$379 million. Together, growth stage deals, as opposed to investments in earlier-stage start-ups, accounted for 77% of quarterly investments, noticeably higher than the average 63% for both in each of the last three quarters. Early stage companies

followed, with 19% of investments, while seed investments accounted for 4% of the capital. With that, seed investments were responsible for more than a quarter of all the deals in Q2/2015.

The stronger emphasis on investments in more mature companies, said Simana, is evidence that Israel's tech economy is maturing – and is seen by many more investors than in the past as a place to make money. “Private equity funds and international conglomerates are the kind of investors we want to see supporting growth companies, and we have lately found that, indeed, the number of growth stage technology companies in Israel is rapidly increasing,” said Simana. “As the number of high growth companies and company valuations climb even further, we expect to see a more diverse investor mix.”

<http://www.israel21c.org/israeli-high-tech-raises-record-1-12b-in-q2-financing/>

'Israeli portfolio companies are priced more reasonably than Silicon Valley companies, making Israel an attractive location for investments and acquisitions.'

New records for Israeli high-tech investments as 179 companies raise \$1.12 billion in the second quarter of 2015, according to the IVC-KPMG Israeli High-Tech Capital Raising Survey. The quarterly amount exceeded former record high \$1.11 billion invested in Q4/2014.

“Fifty percent of the amount raised during this quarter, and even more since the beginning of 2015, results from large deals of \$20 million or more raised per round. The overall number of growth companies attracting investments continues to increase quarter over quarter, reflecting the health of the venture-backed ecosystem in Israel and the patience of investors supporting their portfolio companies to complete homeruns and grow into ‘Unicorns’ that are substantial and mature,” said Ofer Sela, partner at KPMG Somekh Chaikin’s Technology group.

In the first half of 2015, 342 Israeli high-tech companies attracted \$2.1 billion in investments compared to \$1.6 billion raised by 334 companies in the same time frame the year before.

IVC-KPMG’s analysis of investors by type showed that foreign private equity funds and corporate investors were responsible for \$477 million or nearly 43 percent of the total investments in Q2/2015.

“Most of the increase in capital raising in the second quarter can be attributed to two exceptionally large deals, where private equity funds invested in growth-stage companies,” said Koby Simana, CEO of IVC Research Center. “Moreover, an investor profile analysis we conducted shows an impressive increase in the number of foreign private equity funds investing directly in Israeli technology companies – i.e., in deals where the equity capital is placed directly in the company, rather than shareholder equity changing hands.”

Simana says the interest shown by private equity investors in growth stage companies is another indicator of the Israeli technology- and venture capital industry’s evolution and maturity.

“If we want the local high-tech industry to continue growing and see more large-scale, mature companies emerge, there is room for technology investments from more than just VC funds – local or foreign. The industry needs a variety of investors and investment models to support companies throughout various stages. Private equity funds and international conglomerates are the kind of investors we want to see supporting growth companies, and we have lately found that, indeed, the number of growth stage technology companies in Israel is rapidly increasing,” he said.

The software industry led capital raising this quarter with \$487 million (44%) invested in 50 companies. The amount was the largest for the sector.

And, Israel continues to be a top Asian destination for startup investments.

“Investors from Asia are investing in an increasing number of Israeli growth companies, adding to the overall amount of cash available for market expansion,” says Sela. “Overall, Israeli portfolio companies are priced much more reasonably than Silicon Valley companies, making Israel an attractive location for both investments and acquisitions.”