

Investing in: Israel

Israel's high-tech sector is thriving, and now China wants in on the action

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Monday, 15 May 2017 | 1:16 AM ETCNBC.com



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Cars go by on a highway next to Tel Aviv's landmark Azrieli Towers skyscraper complex in Tel Aviv, Israel.

Go to Israel and chances are you'll install some new apps on your phone, just to keep up. A few years ago that might have been the navigation and transportation ones Waze and Moovit. More recently it may well have been photo editors Facetune and Enlight. All Israeli developed, all global successes and just a tip, albeit a visible one, of the country's high-tech iceberg. High-tech is usurping the place once held by Israel's founding myths, the ones about the kibbutz collectives and making the desert bloom. Nowadays it's all "Start-up Nation" and "Silicon Wadi". In fact, some say high-tech is even replacing the archetypal Jewish mothers' wish for their child to be a doctor or a lawyer; today's Israeli moms supposedly brag about the number of employees in their kids' start-up.

Inevitably such success is shot through with hyperbole but it rests on very solid and tangible numbers. \$15.3 billion is one of them, representing the biggest high-tech business deal in Israel's history and the sum that [Intel](#) paid in March for autonomous driving firm Mobileye.

And instead of packing up the company and moving it to the U.S., Intel is establishing it as its global autonomous driving hub and R&D (research and development) center. There are over 300 international firms with a high-tech research center in the country, including giants such as [Microsoft](#), [IBM](#), [Apple](#), Cisco, HP and older Intel centers, to name but a few.

"Over the last couple of weeks, since the Intel-Mobileye transaction, all hell has broken loose," says Jon Medved, CEO of OurCrowd, an Israel-based crowdsourcing platform for accredited investors.



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"The country is being overrun in a positive way by investors, corporations, strategic partners, all sorts, who simply want to get a piece of this."

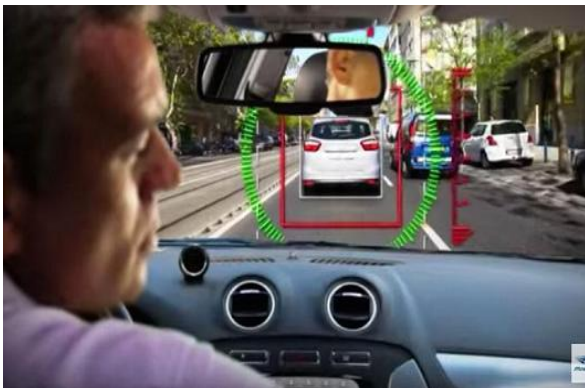
The importance of the deal is also emphasized by Eugene Kandal, CEO of the NGO (non-governmental organization) Start-up Nation Central, which seeks to connect start-ups to investors and supports the Israeli high-tech industry. He headed Israel's National Economic Council until 2015 and was as such a close advisor to Prime Minister Benjamin Netanyahu.

"The message to investors not yet investing is: It's no longer unicorns, it's really big guys," he says.

While those seeking investors in the high-tech industry can be expected to sound upbeat, the message is being repeated by others: The Mobileye deal is big and can be a game changer in terms of making more international companies and investors aware of the potential of Israeli businesses, not just start-ups, where much of the action had often been in the past.

'Israel on the big players' map'

Koby Simana CEO of IVC Research Center, a Tel Aviv-based firm monitoring and analyzing Israel's high-tech industry, says the deal drew international attention. "I think those kind of deals from several hundreds of millions to billions of dollars being spent on one company, that's a big quantum leap for the industry. That puts Israel on the big players' map."



Source: Mobileye

He counts among these mega-deals the \$4.4 billion sale of online gaming company Playtika in 2016 to China's Shanghai Giant Network Technology Co. Playtika is based in Herzliya, Israel, but was owned by U.S. casino and gaming giant Ceasars. This illustrates some of the difficulties in quantifying the number of deals and the amounts involved in Israel's high-tech field. PwC Israel, for example, in its 2016 report on Israeli high-tech industry exits, left out the Playtika deal, noting its ownership by Ceasars. That's how the accountancy firm concluded that in 2016 the value of deals in the industry dropped 51 percent compared to 2015, to \$3.4 billion. PwC's estimate that this was just a temporary slowdown now seems vindicated by the Mobileye deal.

Other big deals since the beginning of the decade include the 2012 acquisition of Waze by Google for over \$1 billion, the 2013 sale of security software firm Trusteer to IBM, for \$1 billion, and Cisco's 2013 takeover of cell phone software firm Intucell for \$475 million.



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The Mobileye deal is certainly big, for Israel. The company does account for some 60-70 percent of the world's autonomous driving and collision avoiding systems but Intel's acquisition is dwarfed by Qualcomm's announcement last year that it is buying Dutch automotive chipmaker NXP for \$47 billion.

Bumper year for venture capital

In terms of venture capital flowing into the industry, Israel had a bumper year in 2016, raising \$4.8 billion in funds, up 11 percent from 2015, according to an IVC-ZAG report. But the same firms note a slowdown in the first quarter of 2017 to \$1.03 billion. That's 4 percent down, or what IVC's Simana calls, "a minor drop".

What concerns the IVC CEO more is the change in the balance of investments, from early stage to late stage, a phenomenon that is also apparent elsewhere, notably in Silicon Valley. The difference is, says Simana, that in the U.S. the volume of investments is decreasing while in Israel it's still increasing. Even so, attracting early stage investment remains important to keep feeding the pipeline of start-ups.

"We call for early stage investors and tell them right now there are opportunities. There's less competition. More risk but less competition," says Simana. "If they want to be in the competitive landscape going forward, they should be in the early stage." The type of investors interested in Israeli high-tech is shifting from North America to Asia, as the Playtika acquisition shows. Chinese investors have discovered the country and PwC in its report also notes that they, "are growing increasingly comfortable with doing deals in Israel." Medved and Simana too notice growing interest from Asia but Simana qualifies this: "Definitely at the moment U.S. and European investors are the dominant ones in the industry."

U.S. interest in Israeli high-tech is long-established and Israeli companies have the third biggest presence on the [NASDAQ](#), after the U.S. itself and China. In the past there has been a perception that many North Americans who invest in Israel do so to support the country. But, says Medved, that's only part of the story: "There's plenty of them but it's way beyond that now. It's just good business. I don't think people are investing emotionally or with their political or religious beliefs as the driver." When it comes to what particular high-tech field to invest in, there's a lot to choose from. According to Kandal of Start-up Nation Central, it's exactly the ability to work across different technologies that makes Israel so competitive. "There are a lot of different sectors. You can be in cybersecurity and digital health. You can be in cars and software. You have enough density for all of those to give you a buzz."



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That's a point that Simana also underwrites: "The big names out of Israel are multi-disciplinary. Take for instance Mobileye, Gett (an Uber rival) or other big names that came out of Israel in recent years. I think the way Israeli entrepreneurs are combining various technologies into one product, one offering is our competitive edge."

Israel's security needs, its lack of water, arable land and its small population, just over 8 million, have all played a role in the development of its high-tech industry. It's long been renowned for its water and agriculture technology, its drone and aerospace industry and its use of solar power. More recent successes include cybersecurity, medical technology, artificial intelligence, machine learning, robotics, and of course transport fields such as navigation and autonomous driving.

Medved, the OurCrowd CEO, says that Israel is especially appreciated for its "deep technology" knowhow. He says investors are attracted because of, "the change in the venture market into frontier technology where the deep tech is now back in fashion, whether it's machine learning, or cybersecurity or drones. Things that need deep technology, that's what makes Israel interesting. We are not leaders in the other stuff but we're leaders in deep technology."

Many of these advances come out of the country's, U.S.-supported and part-financed, military and intelligence establishments and its defense industry. [Some military intelligence units, such as Unit 8200](#), are veritable incubators for the country's high-tech industry, spewing out veterans that are bursting to begin start-ups. And the defense aerospace industry has made the country a leader in drones. But there are also world-class institutes and universities, such as Haifa's Technion and the Weizmann Institute of Science in Rehovot. Israel's R&D expenditure as a percentage of [GDP \(gross domestic product\)](#) regularly tussles with South Korea's for the global top spot.

Risks to the industry

Even the risks to the industry that Israel's high-tech observers mention, can be seen as humble brags. Chief among them is the danger of a shortage of skilled workers, coupled with a decline in the number of pupils choosing science trajectories in high school. It is a real concern and calls have been issued to ease visa requirements for high-tech workers from India and other Asian countries, always a concern in Israel, where demography is a sensitive subject.

Yet, the shortage also sends the message that demand for high-tech workers in Israel is booming. Kandal says that in 2016 there were 1,100 new high-tech start-ups in Israel while 400 disappeared. "It's an indication that people are not afraid to begin new things. If they fail, they just start a new one or go to work at another company that's always looking for people."

IVC's Simana says he has studied the failure rate of start-ups in Israel. "It's one-in-twenty that has a real success. I don't know the numbers but I suspect that's very similar to elsewhere in the world."

It's a sobering reminder that any investment carries risk, particularly in start-ups, however dynamic and attractive the industry. "We're not prophets here," says Simana.

Maybe the most obvious cautionary tale is the one of electric car battery venture Better Place. Its story and that of its founder Shai Agassi were used in the intro to the landmark 2009 book "Start-up Nation: The Story of Israel's Economic Miracle" by Dan Senor and Saul Singer.

Even though it was pushed by Israel's late President Shimon Peres and supported by Nissan's Carlos Ghosn, Better Place went bankrupt in 2013, swallowing up some \$850 million of private capital. It hardly slowed down Israel's high-tech industry, which the same year celebrated Google's \$1 billion-plus acquisition of Waze, but it may have reminded companies and investors that a good idea and lots of "chutzpah" are not necessarily enough to make it in the marketplace.

<http://www.cnn.com/2017/05/15/israels-high-tech-sector-is-thriving-and-now-china-wants-in-on-the-action.html>