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How to invest in the ‘the world’s other Silicon Valley’



The Tel Aviv Stock Exchange. No longer considered an emerging market, Israel produces world leaders in a host of industries. Ariel Jerozolimski/Bloomberg

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They don't call Israel the start-up nation for nothing.

Since Dan Senor and Saul Singer first coined the term in their 2009 book *Start-Up Nation: The Story of Israel's Economic Miracle*, Israel has proudly lived up to its nickname.

The tiny Middle Eastern country of eight million people is a hotbed of entrepreneurial talent, producing some of the greatest inventions in science and technology.

“Israel is the world’s other Silicon Valley,” said venture capitalist Jon Medved, chief executive of equity-based crowdfunding platform OurCrowd, which invests in Israeli and global early stage companies. “It’s the second-most important source of innovation in the world today.”



Israel's Teva Pharmaceutical Industries is the world's largest maker of generic drugs.
Adam Reynolds/Bloomberg

OurCrowd helps investors contribute funds to a business or project in exchange for equity or other tangible but non-monetary rewards. With 18 licenced incubators in Israel, Richard Goodman, head of investment banking at Toronto’s Octagon Capital Corp., said there are plenty of solid options.

“By investing in an incubator or crowdfunding groups, [a retail investor] really has the capability of getting exposure to many more companies than they otherwise would,” he said. “We really like that opportunity.”

Retail investors looking to diversify their portfolios have myriad other options, too.

Money also helps, and Israeli entrepreneurs have little trouble attracting it

No longer considered an emerging market, Israel produces world leaders in a host of industries including technology, health care, agri-tech, biotech, security, consumer products and banking.

Teva Pharmaceutical Industries Ltd., cloud developer Wix.com Ltd., Check Point Software Technologies Ltd., manufacturer Caesarstone Sdot-Yam Ltd. and Bank Hapoalim BM are just some of the names considered leaders in their respective industries.

“You’ve got a diversified economy, but also a very dynamic economy with companies that are operating in a pretty dangerous part of the world, so Israel’s success is nothing short of extraordinary and attributes to the resilience of the economy and the country,” said Steven Schoenfeld, founder and chief investment officer of New York-based BlueStar Global Investors.

Mr. Schoenfeld said investors can choose equities à la carte or through an index-based ETF. The BlueStar Israel Global Index is one benchmark that tracks Israeli public companies trading worldwide, and it’s the underlying index for the NYSE-listed ISRA Market Vectors Israel ETF.

Israel could also soon be a viable source of natural gas for Europe and nearby countries. He urges those thinking about investing in Israel to look beyond the headlines. The country has significantly outperformed U.S. and Canadian equities over the past decade, he said, and most Israeli-based companies generate more than 80% of their revenue outside of Israel “so they’re very resilient and are used to operating on a global scale.”

And don’t be misled by the small size. “Israel may be one of the smallest players on the rink, but it checks and shoots and scores like a top NHL player,” Mr. Schoenfeld said.

Small, as they say, can be beautiful. According to Medved, US\$3-billion will be invested this year in more than 700 Israeli startups, up from US\$2.2-billion in 2013. About 80 companies were bought through mergers and acquisition last year, he adds, and there is “a ridiculous number that go public in New York.”

Six companies went public in New York during the recent Gaza war, he said, including Mobileye, the biggest Israeli IPO of all time. Of the Nasdaq’s non-U.S. listings, Israel boasts an impressive 65 companies — second behind China’s 115 and ahead of Canada’s No. 3 ranking with 45 (there are two Israeli firms listed on the TSX).

As former Israeli president Shimon Peres once said, “Jews are never satisfied because they are always seeking new answers for a better world, a better tomorrow.” And it’s that think-outside-of-the-box, can-do, risk-taking, entrepreneurial attitude that yields 1,100 new startups annually.

There are currently 300 multinational R&D centres in Israel, Mr. Medved said, with 1,000 exits of Israeli startups in the past decade. Much of the expertise is in

semiconductors, telecommunications, Internet infrastructure, data and analytics, and much of the knowledge stems from mandatory conscription.

“The army is very helpful in driving new people into this world because it’s a high-tech army and relies a lot on technology skills and very well-developed analytical skills to help do what it needs to do,” said former Torontonians Ely Razin, chief executive of Israel-based financial data firm CredFi.

“After three years, those people graduate and move into the private sector. So you’ve got this constant push of new people who have been highly trained in related areas, at the expense of the state, and are now available to the private sector.”

Money also helps, and Israeli entrepreneurs have little trouble attracting it. Alan Feld, managing partner of Israel-based Vintage Investment Partners, which manages US \$800-million (about US\$130-million comes from Canadian institutions and family offices), said the amount of money dedicated to investing in Israeli ventures is one-third of what it was during the tech bubble.

But even though “there’s a lot less money chasing companies, especially in the early and mid-stages,” Mr. Medved said that’s good news for investors. Chinese and Japanese companies are now showing interest, too, he adds.

Still, it’s not all rosy. Mr. Razin said the country’s small size makes it imperative for Israeli companies to set up large sales and marketing operations closer to their markets and it can take longer for new industries to erupt.

In the financial technology arena, he adds, few global banks besides Barclays and Citibank have a presence in Israel, though government incentives are being introduced to entice R&D operations.

Of course, there’s always the possibility of war and that can be worrisome to investors. But, as Mr. Medved points out, Israelis know how to multitask.

“We had companies where guys were running jet missions for two days and then running companies for two days,” he said. “Because our wars are relatively short — one or two months max — it doesn’t have a big impact.”

Israel could also soon be a viable source of natural gas for Europe and nearby countries. Natural gas was discovered off the northern coast several years ago, and reports in September indicate the country will be supplying Jordan with a rumoured US\$15-billion worth of natural gas over 15 years. Israel also has one of the top four proven sets of shale deposits in the world.

“The discoveries of natural gas [in Israel] have just scratched the surface,” Mr. Medved said. “The amounts of gas they’re going to find in the eastern Mediterranean basin will be unreal. This has already been the largest single discovery of the decade of natural gas

and they're just getting started. Given Canada's expertise and understanding of this area, I think it's big."

Clearly, the land flowing with milk and honey could also entice more Canadian investing flows.

"There's a golden age now of Israel-Canada political relations — it's never been so good," Mr. Medved said. "Now it's time to match that political warmth with huge economic potential. Given Canada's brain power and access to markets and investment capabilities and the TSX, it's really a very exciting time to be looking at Israel-Canada [investment opportunities]."

"You've got all the pieces of the ecosystem here," said Feld, who moved from Toronto to Israel 20 years ago. "People coming out of the army who are extremely well trained, an experienced venture capital industry, a very broad-based global infrastructure of R&D centres here — Apple, Microsoft, Google, Yahoo, Facebook, etc. — there's entrepreneurship, and you start to build a company global from Day One. All this comes together to create [opportunity]."

There's a brain drain, too, with about 30% computer science graduates heading to Ivy League universities abroad to teach, says Medved. He also worries about three groups that aren't particularly engaged in the start-up mentality: ultra-orthodox Jews and Israeli Arabs (both of whom don't generally serve in the army, which is the breeding ground for start-ups), and women.

Razin adds that companies situated near the Gaza border suffered more disruptions than those farther away during this summer's battle but it didn't bring business to a halt.

"Israelis are very resilient," he said. "Life goes on. There's a mantra here: 'You must live on with your routine.' You just keep pressing on. The way to beat all this craziness is to not pay attention to it. Just go on with your normal life, and people do."

People aren't afraid to fail so they become "serial entrepreneurs" with three or four companies under their belts. "We live in 'Risk Central' so the risk of starting a company is relative to the existential risk we live with," Mr. Medved said.