SIGNIFICANT INCREASE IN INVESTMENT, INCREASING RELIANCE ON A SMALL NUMBER OF COMPANIES, AND A CONTINUED DECLINE IN FOREIGN INVESTORS

THE SECOND QUARTER OF 2024 IN ISRAELI HIGH-TECH

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Introduction

The end of the second quarter of 2024 marks nine months since the launch of the "Iron Swords" war and two years since the beginning of the global economic slowdown. Against this backdrop, the data from the second quarter and the first half highlight several key things:

- After several quarters of stabilization at low levels, and a decline since the start of the war, Q2 actually saw a significant increase in total investment compared to Q1.
- This is not unique to Israel - Europe and the US also experienced an increase in total investment in Q2.
- Total investment continues to rely on a small number of mega-rounds (fundraisings of $100 million or more). Aside from a few companies that managed to raise mega-rounds, total investment was approximately $1 billion. A single investment in Wiz, which raised $965M, constituted 34% of total investment.
- The concerning trend we highlighted in previous reports, of continuous decline in the number of active investors in Israel, both Israeli and foreigners, has continued in Q2.
- Contrary to the impression one can get from several reports, the rate of acquisitions of Israeli technology companies has not increased in 2024. There were 49 acquisitions in the first half of the year, a similar rate to that of 2023 which saw 96 acquisitions.
- A growing concern, especially in the last quarter, is that the international isolation Israel is experience will hurt the high-tech sector. In this report we raise a red flag regarding Israel's innovation and science relations with Europe, focusing on the European framework R&D program.

Unless specified otherwise, the data in this report about Israeli high-tech is based on IVC database. Data for other countries is based on PitchBook database.

Naturally, a report published immediately at the end of the quarter is partly based on provisional data; hence, some of the figures shown in this review may be updated in the months ahead. Where a significant update to the data is expected, we expressly state so.

Recent Publications

- The Israeli AI Landscape
- Israeli High-Tech in the Shadow of War
- The State of Women in Israeli High-Tech | 2024
- What Characterizes Israeli Tech Companies That Raised Money in 2023

1. Investment in Israeli Companies

Having peaked at $9 billion in Q4 2021, investment in Israeli companies has declined almost every quarter since until the beginning of 2023, and then stabilized at a quarterly level of less than $2 billion. After the outbreak of war in Gaza in Q4 2023 investment declined even further, but Q2 of 2024 has experienced a significant uptick.

Figure 1 shows that **the amount in the last quarter is the highest since the end of 2022.** However, it is too early to call it a turnaround, as 34% of total investment was in one company (Wiz), and 64% in mega-rounds of six companies. Excluding these, total investment in Q2 was approximately $1 billion.

Figure 1

Figure 2 depicts the number of investment rounds in Israeli companies, which started to decline in 2022. It is important to note that rounds are often discovered with a substantial delay, and consequently, the data presented here is likely to be revised upwards in the future. But even taking this into consideration, **the trend of continuous decline in the number of rounds has not changed.**

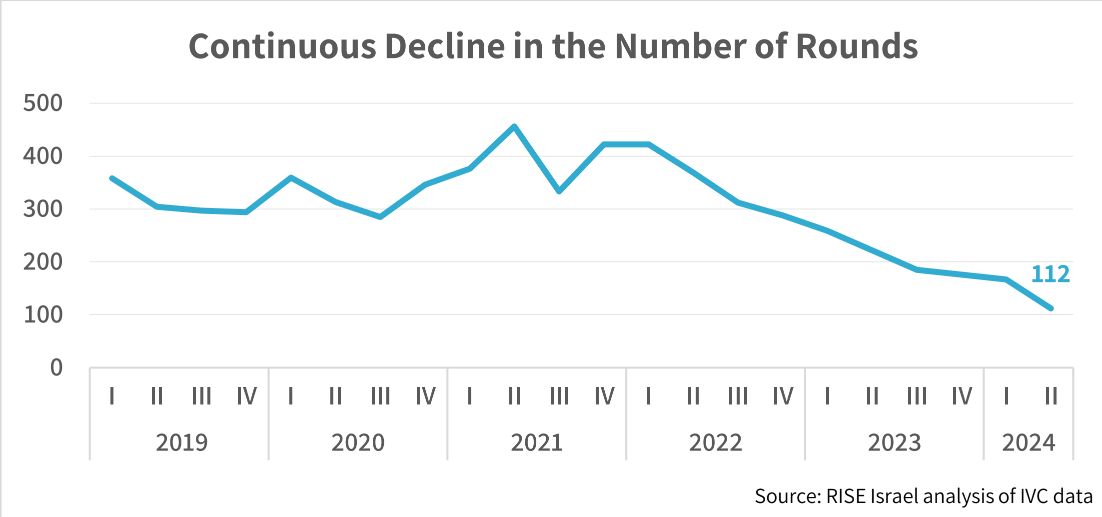


Figure 2

Additionally, the recent difficulty in raising capital drives many startups, particularly in early stages, to utilize Simple Agreements for Future Equity (SAFE) for fundraising. These agreements, which allow companies to secure capital without pre-determined valuations, as well as other forms of fundraising (e.g. internal rounds), are seldom reported publicly, and may lead to underestimation of the investment figures. However, this underestimation is likely consistent with previous quarters.

Figure 3 presents a comparison of total investment in Israel, the United States, and Europe, normalized to Q1 2019. The data indicates an uptick in total investment in all regions in Q2.

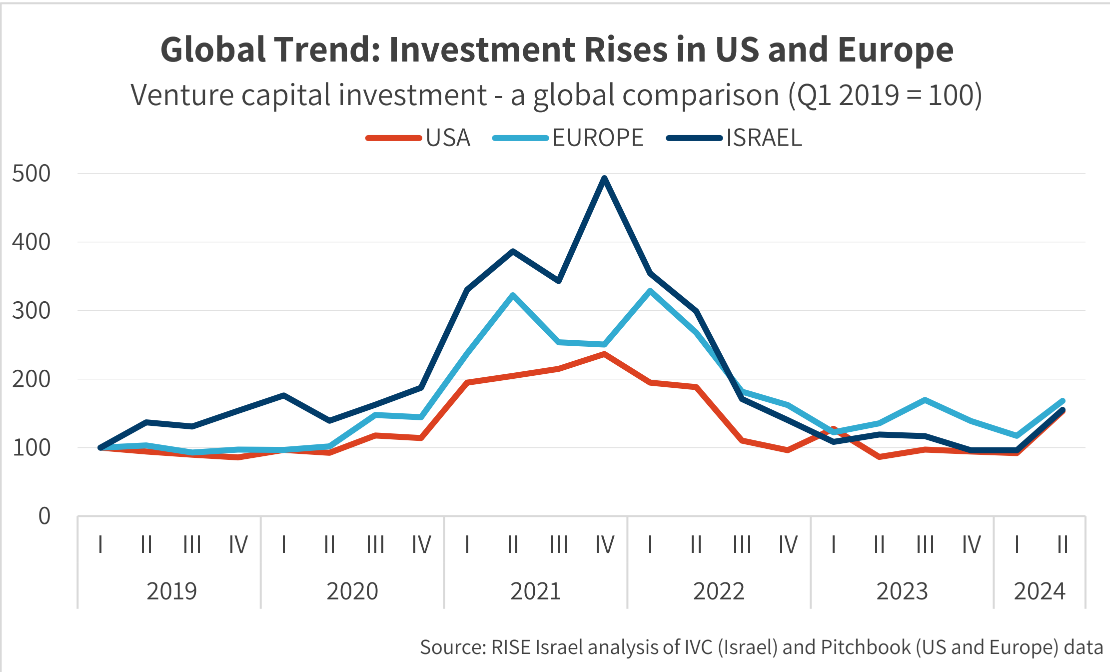


Figure 3

One of the trends in the last quarters is an increasing reliance on “Mega-Rounds” ($100 million or more). **Q2 witnessed six mega-round investments totaling more than $1.8 billion, representing 64% of the quarter's total investment amount**. Excluding these mega-rounds, total investment would have been only about $1 billion. Figure 4 depicts the share of mega-round investment within total investment, and figure 5 describes the quarterly investment excluding mega-rounds. The growing share of mega-investments may indicate that with the exception of a small number of "star companies", the broader high-tech sector is facing difficulties raising money.

Of the six companies that raised mega-rounds:

- Three are in the cyber sector, two in enterprise software, and one in life sciences.
- All six have a US-based headquarters. One of them also has an Israeli one.
- Two companies became unicorns in the last round and four had this status before the last round.

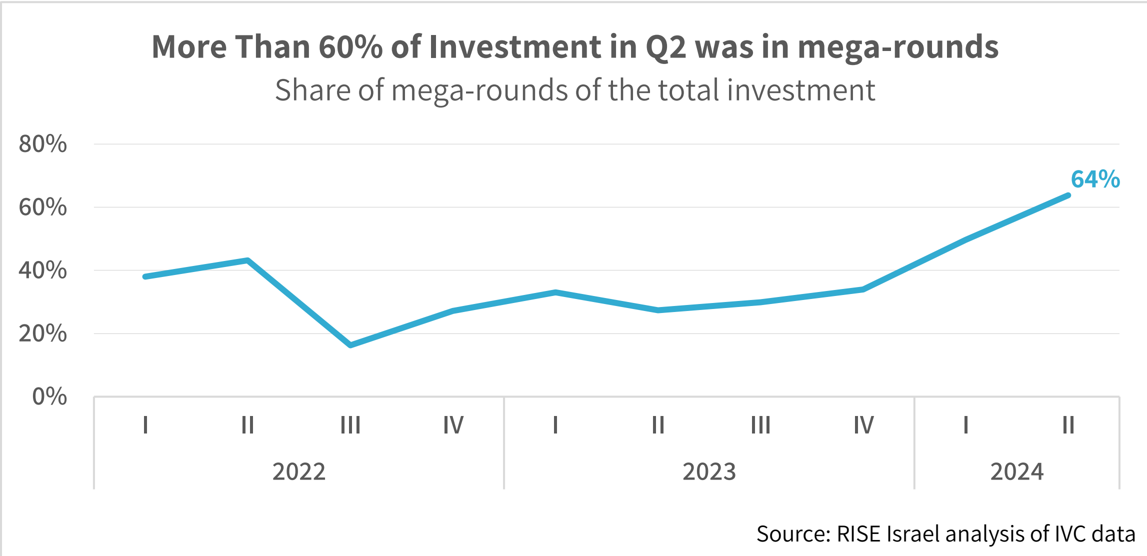


Figure 4

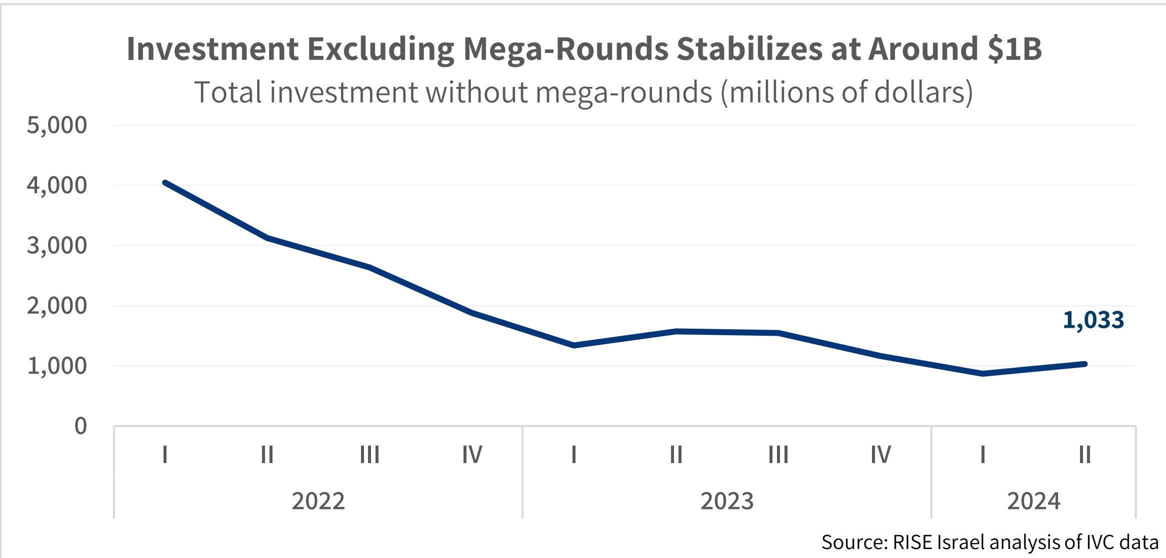


Figure 5

Implications

The trend of increased dependence on a small number of mega-rounds continued in Q2. It seems that the broad high-tech sector continues to face challenges raising money. While this level of a few high-performing companies could be sustainable, the total level of investment will likely depend on their number and the amounts they manage to raise.

2. Investors in Israeli Companies

In our recent reports, we highlighted a concerning decline in the number of active investment entities in Israel, both local and foreign. As can be seen below, **this trend continued into the first half of 2024**. Since the decrease in the number of active investment entities began in 2022, it is unclear how much of it stems from the global slowdown that started in that year, how much was influenced by the internal instability and the war that characterized 2023, as well as the worsening sentiment towards the State of Israel in various countries at the beginning of 2024. Additionally, it is plausible that at least part of the decline in activity of local entities is due to their own difficulties in raising capital.

Figure 6 compares the number of active investment entities (i.e., those that made at least one investment and are not private individuals) - venture capital funds (VC), corporate venture capital funds (CVC), institutional investors, and corporations – in a half-year breakdown, separating foreign and Israelis. During the first half year of 2024, there was a decline of 10% in the number of active **foreign** investment entities in Israel compared to the six months prior, and a 18% decline compared to the first half of 2023. As for **Israeli** investment entities, the declines were 15% and 22% respectively.

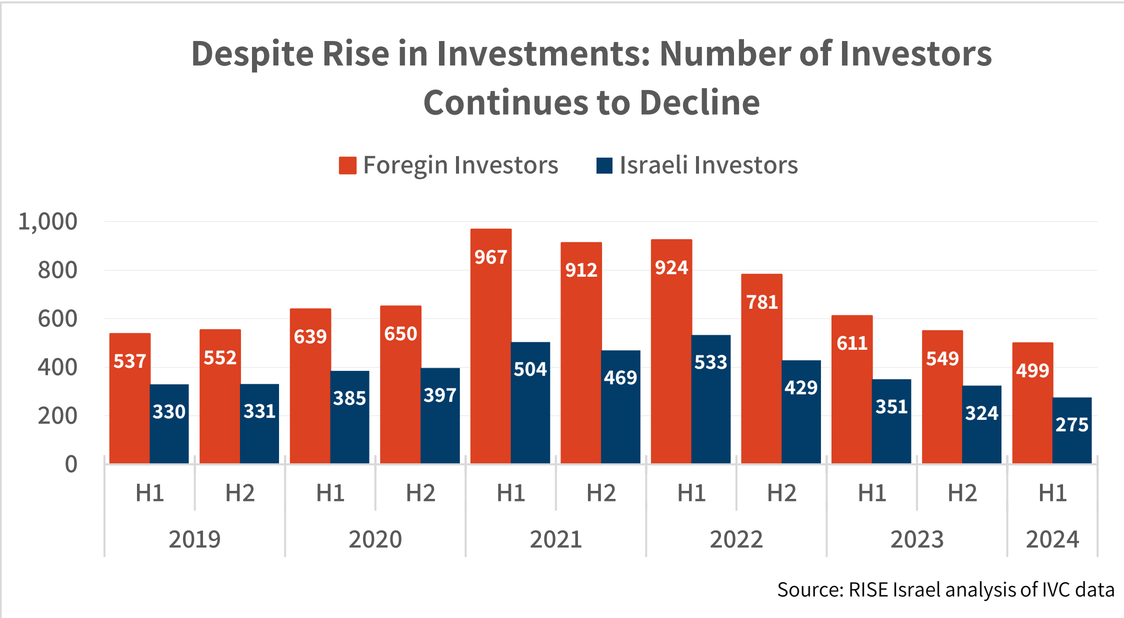


Figure 6

Figure 7 compares the number of active venture capital funds in a half-year breakdown, separating Israeli and foreign funds. The data show that during the half year of the war, the number of active **foreign** funds in Israel decreased by 11% compared to the previous six months, and 15% compared to the first half of 2023, while the number of **Israeli** funds decreased by 16% and 15% respectively.

Approximately 70% of the active foreign investment entities and of the active foreign VC funds in Israel in 2024 are US-based, highlighting the importance of Israel's relations with this country.

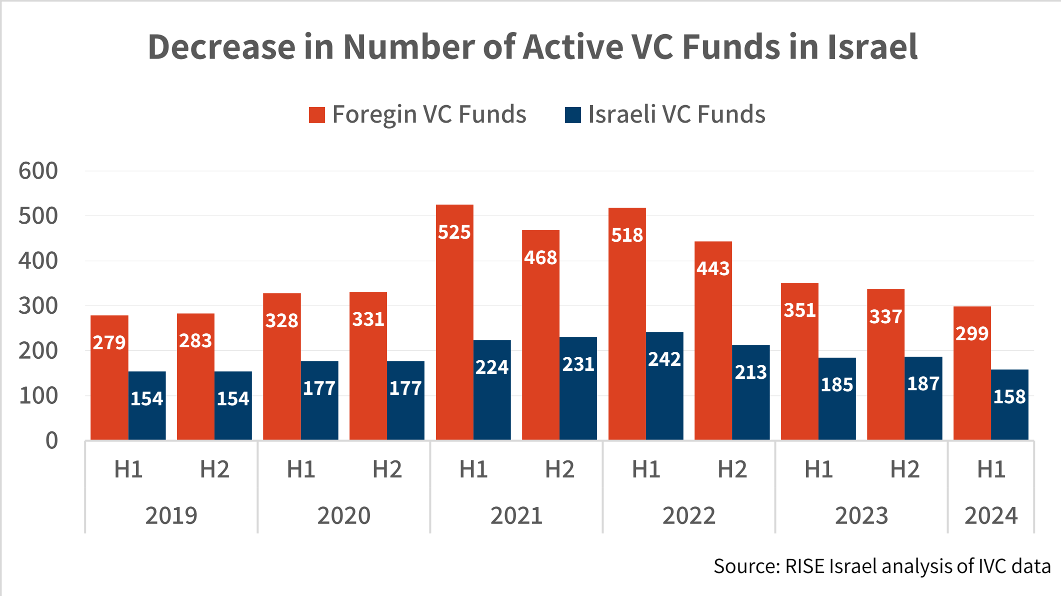


Figure 7

Implications

As mentioned above, it is unclear what exactly caused such a significant decrease in the number of active investing organizations in Israel. Among the possibilities:

- Some investors reduced their activity due to the global economic slowdown.
- Some funds themselves are struggling to raise capital, affecting their investment activity.
- Fewer attractive companies for investors are being established or are operational in Israel.
- Some investors invested only in internal rounds, which were not reported publicly .
- Some investors have stopped investing in Israeli companies due to reasons related to the political and security situation in Israel, or due to a deterioration in sentiment towards Israel.

Regardless of the reasons for this decline, **the phenomenon is extremely concerning.** The Israeli high-tech sector needs both the establishment of new startups and the opportunity for growth and expansion of more mature companies, requiring an active ecosystem of investment entities, both local and foreign. The decline in the number of foreign investors is very worrying, as it may indicate a trend of distancing from Israel due to recent events. The same goes for Israeli VC funds, as it may indicate their difficulty in raising capital. **Since most of the money for Israeli funds comes from foreign sources, their difficulties in raising capital could also indicate a distancing of foreign investors from Israel.**

3. Exits

In recent months there has been much talk about the number of exits of Israeli technology companies, sometimes portraying them as a positive indication of the state of the high-tech sector. It is important to clarify the topic and the data.

Exits typically fall into two main categories – Initial Public offering (IPO) and acquisition by another entity. An IPO is usually positive. The company demonstrates meeting the legal and business requirements of the exchange where it goes public (most Israeli companies do it on New York's NASDAQ, but there are other examples too), it raises money from the public, and continues to operate as an independent company.

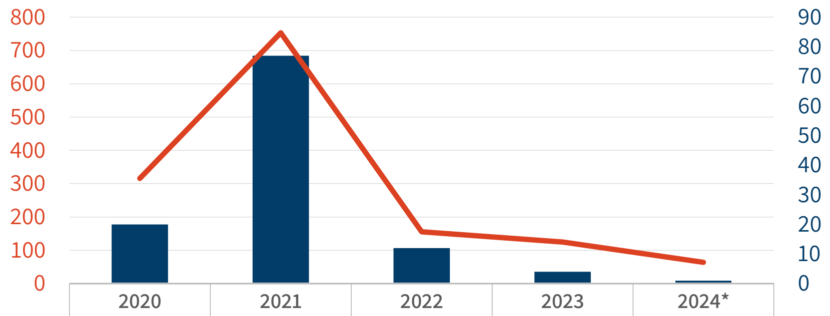
An acquisition on the other hand, isn't necessarily "good". Moreover, there is no clear definition of a "good acquisition", as it depends on factors like the acquisition price compared to the acquired company's past valuation, whether the acquisition creates a profit to entrepreneurs, investors, all or some, the alternatives to the acquisition, what will happen to the company and its employees post-acquisition, etc.

We can examine two of the largest acquisitions of Israeli companies in Q2 – the acquisition of NoName Security by US-based Akamai, and the acquisition of WalkMe by Germany's SAP. In both cases the acquisition price was very high ($450 million and $1.5 billion respectively), and in both cases the acquirer is a large international technology company, which demonstrates in the acquisition faith in Israeli technologies and talent, and a willingness to expand operations in Israel during these challenging times. At the same time, Noname Security's valuation in its last funding round in December 2021 was $1B, and WalkMe went public in June of that year at a valuation of $2.5B, so at least some of the investors in these companies lost money on their investments.

It is therefore impossible to assess the "goodness" of exits. In this chapter we will present some interesting data about exits starting in 2020.

Figure 8 depicts the number of IPOs of Israeli technology companies, the share of IPOs within all exits, and the total number of IPOs on New York-based NASDAQ, which is usually the preferred exchange for technology companies. 2021 was a record year for high-tech globally, and the ensuing decline in the number of IPOs is not unique to Israeli companies.

Not Just Israeli Companies: Number of NASDAQ IPOs Declining



	2020	2021	2022	2023	2024*
Share of IPOs within all Israeli exits	12%	27%	8%	4%	2%
Number of IPOs of Israeli Companies	20	77	12	4	1
Total number of IPOs on New York-based NASDAQ	316	753	156	125	64

Source: RISE Israel Analysis of NASDAQ and IVC Data

*Data for the First Half of 2024

Figure 8

Figure 9 compares between the total number of Israeli technology companies IPOs (in all exchanges) and the total number of NASDAQ IPOs, both normalized to the number in 2020. While trends are similar, the decline in the number of Israeli IPOs in 2023 was sharper.

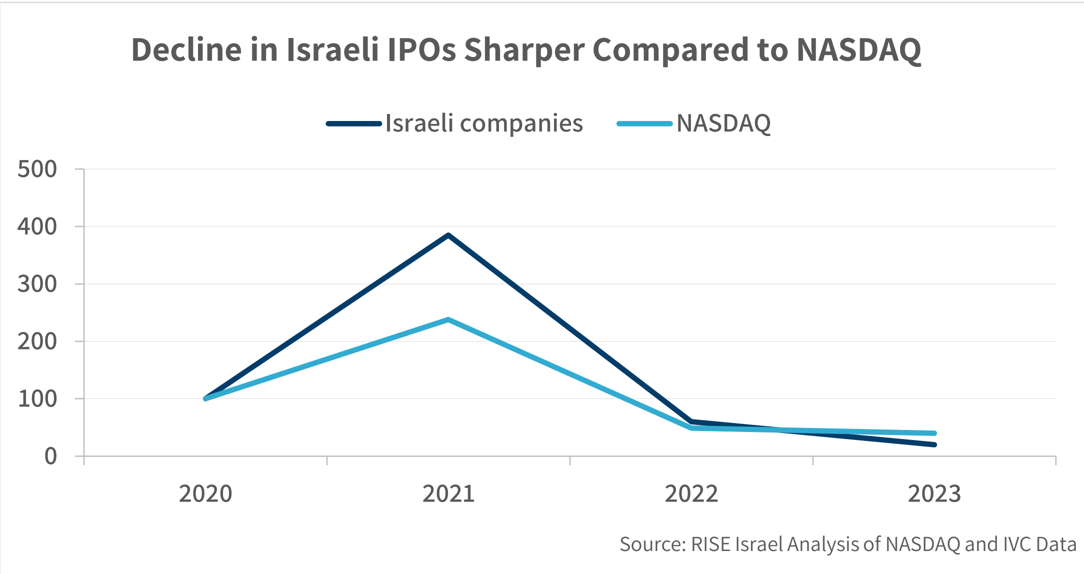


Figure 9

While 2024 numbers are obviously partial, so far the total number of NASDAQ IPOs stabilizes, and even trends up compares to 2023, the number of Israeli IPOs keeps declining. So far only one Israeli company (Gauzy) went public.

Acquisitions

Table 1 shows the number of acquisitions of Israeli technology companies. Contrary to the sentiment conveyed by some reports, the rate of acquisitions in 2024 has not grown, and it is quite similar to that of 2023. Obviously, maintaining the pace during a time of war is an encouraging sign.

	2020	2021	2022	2023	2024*
Acquisitions	150	209	137	98	49

*Table 1 - *Data for the First Half of 2024*

Figure 10 depicts the breakdown of acquisitions of Israeli technology companies in 2024 by sector.

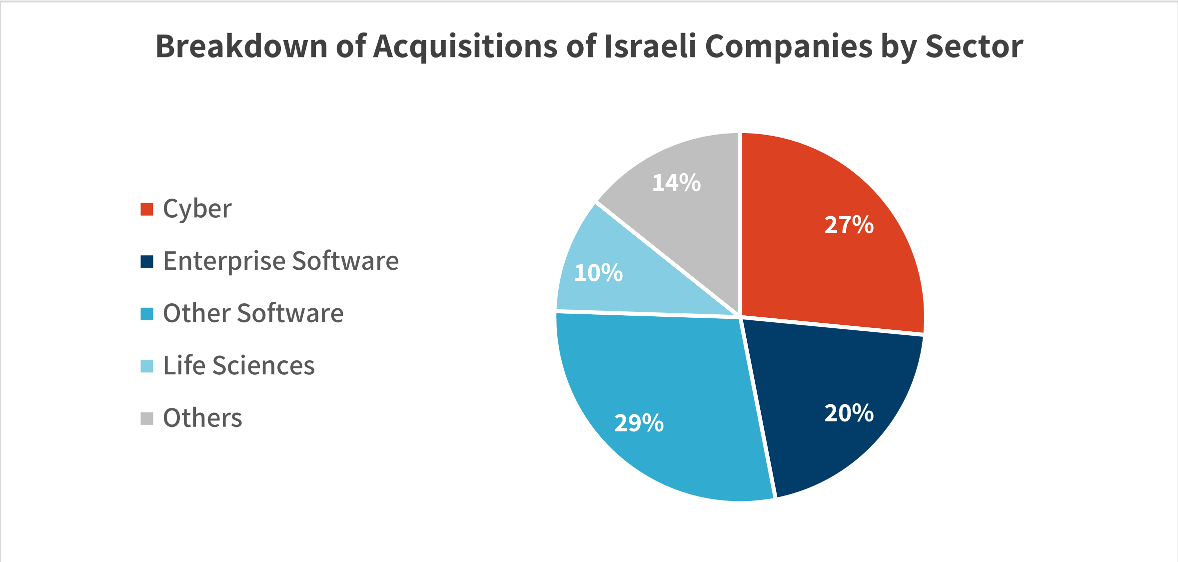


Figure 10

4. Innovation and Scientific Relations with Europe

A report on the current status of Israeli high-tech cannot ignore what is happening in Europe. Banning the participation of dozens of Israeli defense companies in the Eurosatory trade show in Paris was broadly covered in the media, but this is potentially just the tip of the iceberg. The main problem, which may worsen, relates to participation of Israeli entities in the Horizon Europe R&D program.

As background, Israel is one of 18 association countries in the European program, along other countries that are not full EU members, including the UK, Norway, and Turkey. As an association country Israel can participate in Europe's R&D programs, and it has done so since 1996. The current program, Horizon Europe, was launched in 2021 with a budget of more than 90 billion Euro over seven years (through 2027). To grasp the significance of Israel's participation in these programs, below are some interesting facts:

- Since Israel joined the European programs, Israeli entities, including academia, technology companies, and others, have received **grants of approximately 3.15 billion Euros**.[1]
- Of this amount, more than 1.9 billion Euros were granted to seven academic institutions (Weizmann Institute, Hebrew University, Tel Aviv University, Technion, Bar Ilan, Ben Gurion, and Haifa Universities) for research.
- In the previous program, Horizon 2020m between 2014 and 2020, Israeli entities received grants of 1.28 billion Euros.
- So far, in Horizon Europe, Israeli entities were granted more than 600 million Euros.
- In 2023, Tel Aviv University and the Hebrew University were among the top ten universities in terms of grants received, each receiving approximately 50 million Euros.
- 34 Israeli technology companies, mostly in healthcare, received grants and investments from the EIC (European Innovation Council) Fund.[2] This fund was launched by the European Commission in 2020 with a budget of more than 10 billion Euros, for early investments in promising deep tech companies, to allow them to advance to a stage where they are more attractive to "traditional" investors, as investment risk is reduced.

Beyond the significant financial value of participation in the programs, participants also benefit from collaborations with other researchers, academic institutions and companies from across Europe and from better access to this market.

Recently there are some worrisome indications about Israel's participation in the program:

[1] https://dashboard.tech.ec.europa.eu/qs_digit_dashboard_mt/public/sense/app/1213b8cd-3ebe-4730-b0f5-fa4e326df2e2/sheet/0c8af38b-b73c-4da2-ba41-73ea34ab7ac4/state/analysis

[2] https://discover.dealflow.eu/lists/18826/list/f/slug_locations/anyof_israel?selectedColumns=name%2ChqLocations%2CgrowthStage%2CcompanyMarket%2Ctype%2ClastFundingEnhanced%2CtotalFunding%2CcompanyEmployees%2ClaunchDate%2CstartupRankingRating&showGrid=false&showTransactions=false&sort=-startup_ranking_rating

- The EU Foreign Affairs Council decided in a meeting on 27 May to call a meeting of the Association Council, which governs the relations with Israel. Part of the discussion in that meeting was about sanctions on Israel, though several EU countries oppose such sanctions. The Association Council will discuss the situation in Gaza, and whether Israel is fulfilling the human rights obligations of the association agreement it signed in 2021.[3] The first part of this agreement mentions "the importance which the Parties attach to the principle of economic freedom and to the principles of the United Nations Charter, particularly the observance of human rights and democracy, which form the very basis of the Association".[4]
- An increasing number of European universities announced they would no longer collaborate with Israeli entities, and some even suspended their participation in collaboration programs that are already underway.[5]

Collaborations with European researchers, universities, and companies have a big strategic value for Israel, and especially for the high-tech sector. In addition, participation in Horizon Europe provides significant funding for R&D, at a time when raising money by technology companies is extremely difficult, and when due to the Gaza War the government will not be able to increase its spending on R&D in the foreseeable future. Any sanctions on Israel, whether de jure or de facto, will greatly hurt Israel's innovation ecosystem, during a period of rapid global developments in technologies such as artificial intelligence. Most projects in the European program are based on collaborations between several entities from several countries. **Boycotting Israeli entities by entities from other countries, will shut Israel out of the program even without formal sanctions.**

[3] net/news/horizon-europe/eu-convenes-key-israel-council-gaza-boycotts-spread

[4] https://eeas.europa.eu/archives/delegations/israel/documents/eu_israel/asso_agree_en.pdf

[5] https://sciencebusiness.net/news/universities/academic-boycotts-over-gaza-war-jeopardise-israels-place-horizon-europe

Summary and Recommendations

Needless to say, the most important things for Israeli high-tech are returning to a security and political stability, rehabilitation of Israel's image where it was damaged, and in general – reestablishing Israel's image as an attractive place for investors.

Nine months after the breakout of the war, with assessments that it may continue at various intensity levels for a long time, and in the shadow of the uncertainty in the North, one cannot regard the current challenges of the high-tech sector, as sort-term only. While in some ways the sector demonstrates admirable resilience, the stabilization of non-mega-round investment at a quarterly level below $1 billion, and the continuous decline in the number of active investors in Israel, are reasons for concern. The Government, mainly vis the Innovation Authority, must find ways to help good start-ups survive this period of uncertainty.

Regarding the Horizon Europe program – combative statements by Israeli politicians against European entities will not help, and will likely cause damage. It is imperative to maintain dialogs with European companies and academic institutions not about the war, where we are unlikely to convince them, but rather about Israel's significant contributions in past European projects in promoting health, sustainability and welfare both in Europe and globally.