
The Number of New Israeli Startups is Declining For a Decade, Is This a Problem?



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Background

Startups are an important part of the high-tech sector in Israel. Although, like everywhere else in the world, most of them do not survive in the long term, some develop and become large companies or are acquired by other companies. At the same time, they provide high-productivity employment both for R&D personnel and for professionals in other fields (product, marketing, finance, human resources, etc.), whether through direct employment or outsourcing. In addition, startups help increase foreign investments in Israel, as the capital they raise usually comes from foreign sources, either directly (foreign investment in a company) or indirectly (investment by an Israeli fund that raises funds from foreign parties). Furthermore, new startups tend to adopt innovative technologies and business models faster than established companies – thus forming an important pillar in the technological and business front of Israeli high-tech.

However, despite Israel's image as a startup nation, in the last decade, there has been a continuous decline in the number of new technology companies founded in Israel each year. This report addresses this phenomenon and its implications. Key findings:

- The trend of decline in the number of new startups continues.
- The primary decline is in software fields, in which Israel has traditionally excelled.
- There is no indication that, alongside the decline in the number of new startups, there is an increase in the quality of those that are founded.

From this, we conclude that the ongoing decline is negatively impacting long-term employment opportunities in the high-tech sector, where productivity and salaries are high, as well as IPOs and acquisitions of Israeli companies. We believe this requires clear policy measures.

In recent weeks, there have been suggestions that the number of startups actually founded in 2024 is unusually high compared to the known number, as for various reasons, entrepreneurs and investors have higher interest in keeping the company's establishment confidential. Even if this is true, it is quite clear that the decline continues this year as well, and in any case, **the downward trend has been ongoing for a decade.**

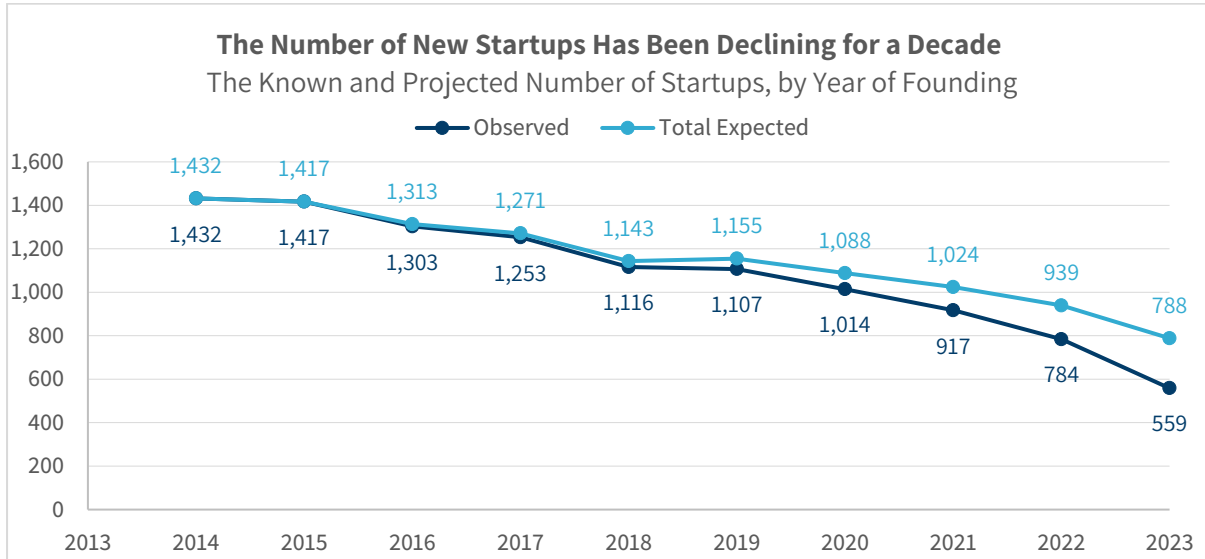
Unless otherwise specified, the data in this report is based on the IVC database.

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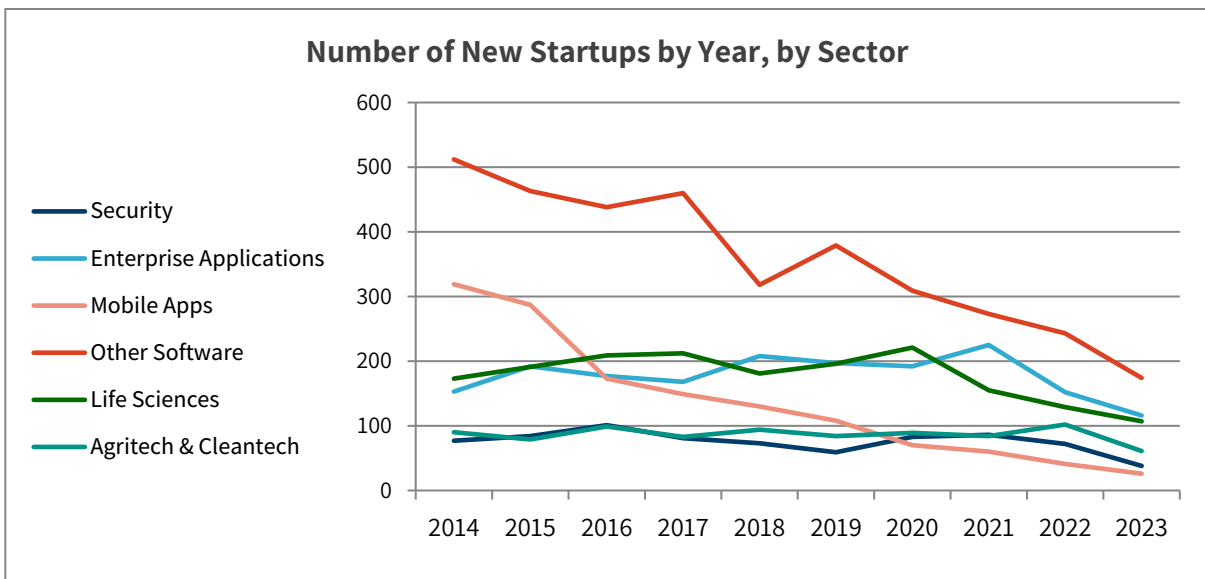
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Number of new startups

Chart 1 shows the number of startups founded in Israel each year over the past decade. It is important to note that new companies are often discovered long after their establishment, which is why we present in the chart both the data known today and the expected data based on historical analysis of the rate of discovery of new companies. The data for 2024 indicates a continued decline, but since the year has not yet ended, and due to the reason mentioned above, we have chosen not to present this data for now.



An analysis of new startups by sector reveals that while cyber, enterprise software, life sciences, agritech and clean-tech are quite stable, mobile applications and other software fields experience a continuous and sharp decline (see Chart 2).



It is very likely that a large part of the decline in the number of new startups in mobile applications or in certain sub-sectors of software is due to the fact that innovation waves in these areas have reached a low point, and there are not enough new opportunities. At the same time, it is also clear

that there is no growth in the number of new startups in Israel in other fields, such as life sciences, agritech, and cleantech. Additionally, it seems that the global AI revolution has not yet led to an increase in the number of startups in Israel.

It is difficult to accurately assess the reasons for the continuous decline, but there are several possible explanations:

- As mentioned above, **some of the innovation waves that enabled the founding of many companies have passed**. For example, in 2014-2015, many companies were founded in fields like digital commerce and mobile applications. These fields did not require unique technological innovation or large initial investments, so the entry barriers were low. Over the years, these fields consolidated, and few new opportunities remained. Subsequent waves of innovation were characterized by higher entry barriers.
- **Some of the recent innovation waves favor large companies and disrupt the startup world**. Generative AI (GenAI) is a prominent example in the last two years. Part of the disruption is due to the fact that a particularly large initial investment is required in this field, and part of it is because large companies offer products or services for free, making it economically unfeasible for startups to profit in this space. As noted, this phenomenon has been particularly evident in the past two years, but it is important to mention it in this review because it could contribute to a continued decline in entrepreneurship in the future.
- Large technology companies in general, and Israeli development centers of multinational companies in particular, offer excellent working conditions and opportunities to work with the most advanced technologies, thus **providing a safe and attractive alternative to working at startups**. It is important to note that even if part of the motivation for some entrepreneurs is a genuine passion for starting a startup and they do not wish to work at large companies, they still need to recruit additional team members, and as mentioned, these people have attractive alternatives.
- **The increase in salaries in high-tech in recent years has led to startups needing significantly higher initial investment amounts**, as early-stage expenses are mainly on salaries. Salary increases also make it even more difficult to compete for employees with large companies.
- In the past couple of years, both due to the global slowdown and specific events in Israel, such as the instability caused by the judicial reform and the war, many companies are struggling to raise capital. **This difficulty affects the motivation of potential entrepreneurs to start new companies**, knowing that at some point, they will need to raise capital.

Is This a Problem?

Some believe that the number of new startups in Israel in the past was too high, and that during those years, low quality startups were founded. To examine whether there has indeed been a trend of moving from quantity to quality in the last decade, we analyzed the percentage of companies founded each year that met the following "quality" criteria:

- Currently employ 25 or more employees.
- Currently employ 100 or more employees.
- Raised 25 million dollars or more since their founding.
- Raised 50 million dollars or more since their founding.
- Went public.
- Were acquired for 100 million dollars or more.

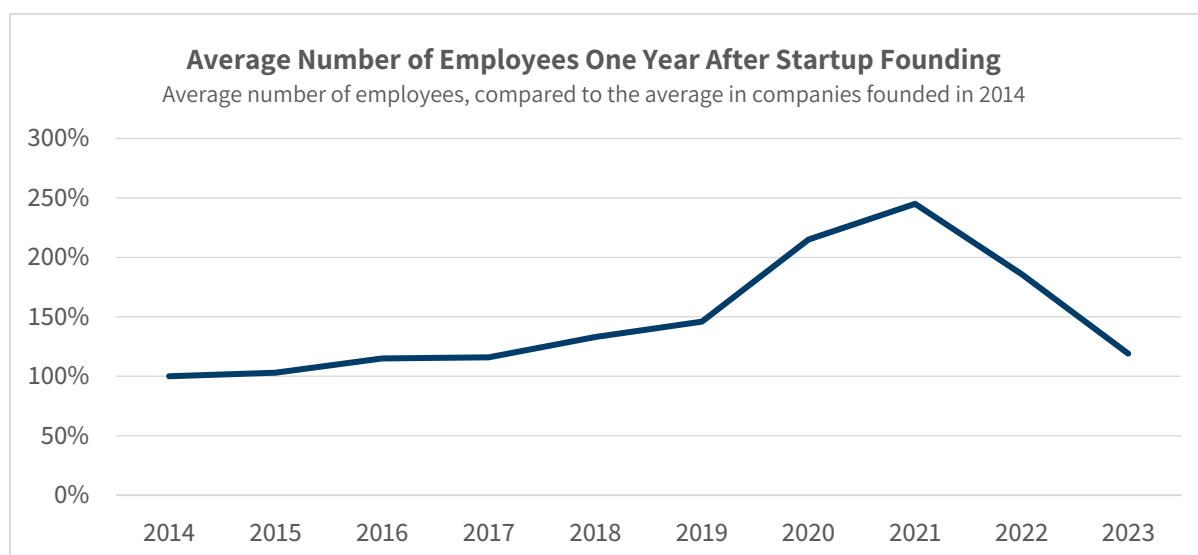
The data is summarized in Table 1. Naturally, the data for 2023, and even for 2022, should not be given much weight, since it takes time for companies to reach these milestones, especially during crisis periods like the past two years. It is highly likely that their percentages will rise in the future. However, the table shows no signs of a shift from quantity to quality, as the percentage of companies meeting these criteria has not increased over the years, and in many cases has decreased. Even if these percentages rise in the future, they will likely only return to historical levels.

Year of Founding	Employ 25 or More Employees	Employ 100 or More Employees	Raised \$25 Million or More	Raised \$50 Million or More	Went Public (IPO)	Were Acquired for \$100 Million or More
2014	14.6%	4.1%	5.6%	3.1%	1.3%	1.2%
2015	15.7%	5.2%	6.8%	5.2%	1.0%	1.2%
2016	15.7%	3.6%	6.1%	3.7%	1.0%	0.7%
2017	15.2%	3.9%	7.3%	4.7%	0.6%	0.6%
2018	15.6%	3.6%	6.2%	3.6%	0.6%	0.8%
2019	14.8%	3.0%	5.7%	3.1%	0.3%	0.5%
2020	15.1%	1.5%	4.2%	2.2%	0.1%	0.6%
2021	14.1%	1.7%	3.7%	1.3%	0.1%	0.6%
2022	10.3%	1.2%	2.4%	1.2%	0%	0.4%
2023	4.5%	0.7%	0.5%	0%	0%	0.2%

Table 1

It is known that at different times there are differences in the difficulty startups face in raising capital, the valuations that investors are willing to assign to companies, and the terms of investment. However, Table 1 shows that at no time have investors compromised on the quality of the startups they invest in, and there is no indication of a higher proportion of "bad" companies at any point in time.

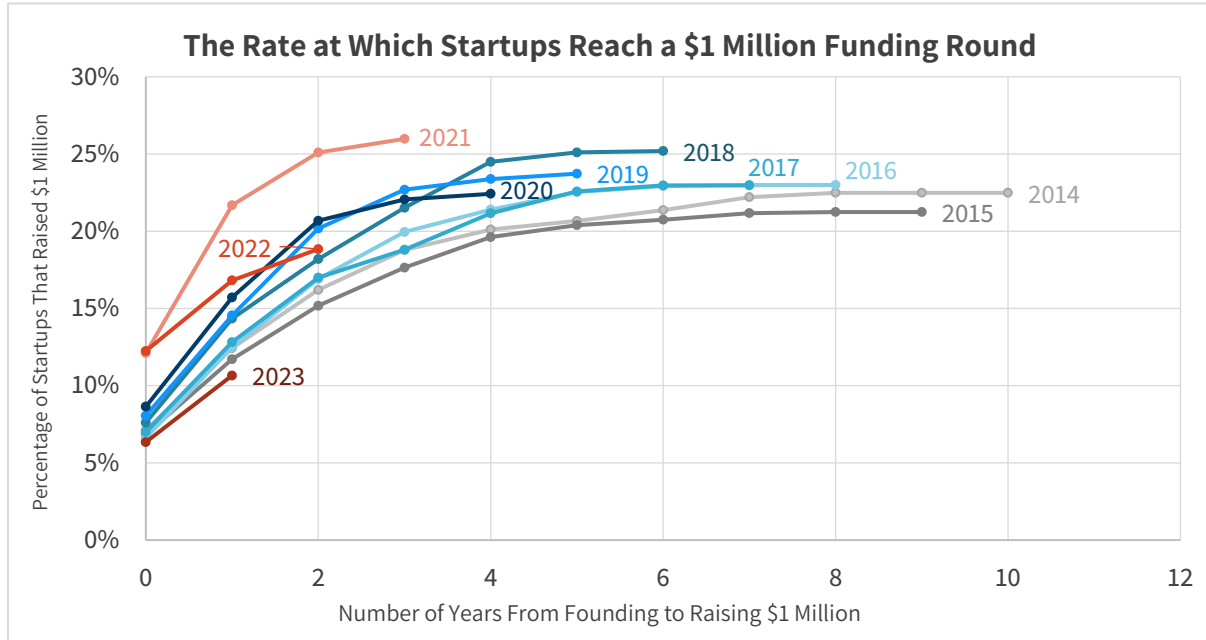
Table 1 presents the current snapshot, but does not show a change over time. Therefore, we also analyzed such changes. In Chart 3, the horizontal axis represents the founding year, and the vertical axis shows the average number of employees one year after founding. The chart is based on an analysis of LinkedIn data¹, and due to certain limitations related to this analysis, we show the average number of employees relative to the average number in 2014. Between 2014 and 2019, there was a stable funding environment. Therefore, the moderate increase in the average number of employees one year after the company's establishment during that period could perhaps indicate a shift from fields like online advertising or mobile applications, where a small number of employees was required, to fields with more technological depth, where more employees are needed. Such a shift could partially explain the decline in the number of startups as related to different technology waves – fewer but larger startups.



However, the chart suggests that the most significant factor affecting the number of employees is the difficulty or ease of raising capital. In 2021 and part of 2022, startups found it easy to raise capital, and they took advantage of the large amounts of money they raised to hire people. The decline in companies founded in 2022 and 2023 is likely due to the difficulty of raising capital in those years. Therefore, it cannot be concluded from this analysis that the decline in the number of new startups is, even partially, a result of a shift between sectors.

¹ The LinkedIn profiles have been collected by the Initiative Bright, and made available to us for research purposes. We thank Initiative Bright by Bright Data for their generosity.

We also examined the rate at which startups reached the milestone of raising one million dollars. In Chart 4, the horizontal axis represents the number of years since founding, the vertical axis shows the percentage of startups that raised one million dollars, and each graph represents startups founded in a specific year.



For example, let's examine the percentage of startups that raised \$1M two years after their founding (one time point in chart 4):

	2014	2015	2016	2017	2018	2019	2020	2021	2022
Raised \$1M in the First Two Years	16%	15%	16%	19%	18%	20%	21%	25%	19%

Table 2

Although it seems that, in general, companies founded in later years reached this milestone earlier, it is likely that those founded in 2021 simply benefited from the ease of raising capital that year. Additionally, even if there is indeed an improvement in the ability of new companies to get funding, which may indicate an improvement in their quality, this improvement is very moderate compared to the sharp decline in the number of new companies.

Assuming that eventually, even the companies founded in 2022 and 2023 will reach "normal" levels, it can be said that out of every 100 new startups founded in Israel, 14-16 will eventually employ more than 25 workers (with high salaries and productivity), and 3-5 will employ more than 100. The absence of these companies will prevent the creation of jobs accordingly. Additionally, out of every 100 startups, 6-7 will raise 25 million dollars or more, and 3-5 will raise 50 million dollars or more; one company will go public, and one will be acquired for more than 100 million dollars. A decline of several hundreds of new startups will double these numbers accordingly.

Summary

Startups play an important role in Israel's high-tech sector. Over the past decade, there has been a steady decline in the number of new startups founded each year, and this is not due to a "shift from quantity to quality," as there has been no improvement in the "quality metrics" of startups. Entrepreneurs and investors are generally rational, so there is no reason to believe that anything is causing or will cause an increase in the proportion of "bad" startups being established or receiving funding at any given time. Therefore, it is important to assist entrepreneurs and investors as much as possible in early-stage rounds and to remove any barriers they face.