

Israel VC Indicator Survey.

Expectations as of Quarter 1, 2010

Forming Alliances?



About

The purpose of the Israel VC Indicator Survey is to identify trends within the venture capital arena. Its objective is to give a comprehensive picture of the Israel VC community expectations for the next six to twelve months. The survey is designed to explore relevant key aspects, such as economic and market conditions, deal activity and investment and managerial focus. The results produce a forward-looking measure of the overall sentiment in the Israeli venture capital community, which is extremely relevant to immediate deal flow.

The 32nd Deloitte Brightman Almagor Zohar Israel VC Indicator Survey results for Quarter 1, 2010 include a comparison, to responses from previous surveys.

The VC Survey and Private Equity Surveys are a Deloitte initiative. The surveys have been conducted for some years, running concurrently in Israel, the United Kingdom, Germany, Spain, Portugal, Central Europe, Mexico, South Africa and India, to name but a few. Moreover, once a year, Deloitte also releases a Global VC Survey, whose purpose is to identify attitudes of venture capitalists and private equity investors regarding investing on a global basis and tracking long-term trends about the attitudes of international investing.

Responses for Israel VC Indicator Survey Quarter 1, 2010 were collected from March 17th, 2010 to March 28th, 2010. The responses were collected from venture capitalists in Israel.

Deloitte Technology, Media & Telecommunications Business Development Team uses a variety of research and statistical tools to provide extensive and accurate analysis of the survey results. If respondents do not answer a question, the count for the question is adjusted accordingly. All charts presented in this report are sourced from the survey results.

First Quarter, 2010

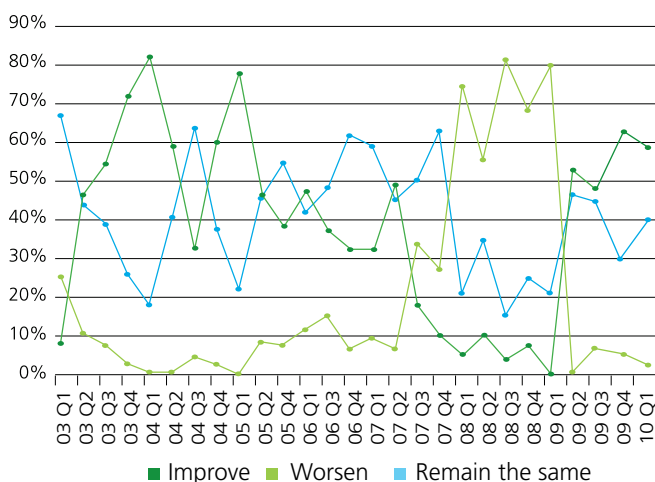
Highlights

- Continuing improvement in venture capital sentiment is gaining momentum
- Early investments are beginning to reflect pre-crisis levels
- Increasing optimism geared towards 2010 to unfold as Israel's first IPO on NASDAQ
- Hype in the Life Science grows whereas Semiconductor continues to falter
- Signs of hope regarding Arab-Israeli market and collaboration

Results

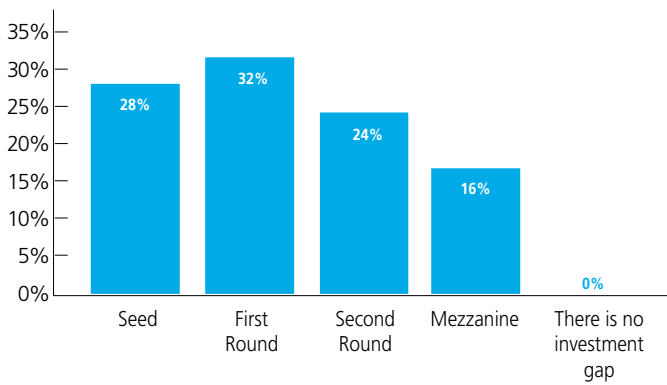
The general perception amongst respondents indicated a continuation of improvement in market sentiment. With a hefty 96% of respondents claiming that the overall economic climate will continue to drive forward or remain the same projects the full 180 degree shift from the levels seen during the financial crisis. It is essential to note that Q1, 2009 forecast for improvement was a staggering low 0%, whereas Q1, 2010 is 58%. This is in parallel to only 4% of venture capitalists today forecasting economic climate to worsen compared to 79% in 2009. Respondents expressed a 7% QoQ increase in forecasts for economic climate to remain the same, in parallel to a decrease of 2% QoQ of participants believing the market to worsen, also reveals a greater proportion of respondents expressing that the worst is behind them.

Chart 1: During the next six months, I expect the overall economic climate to:



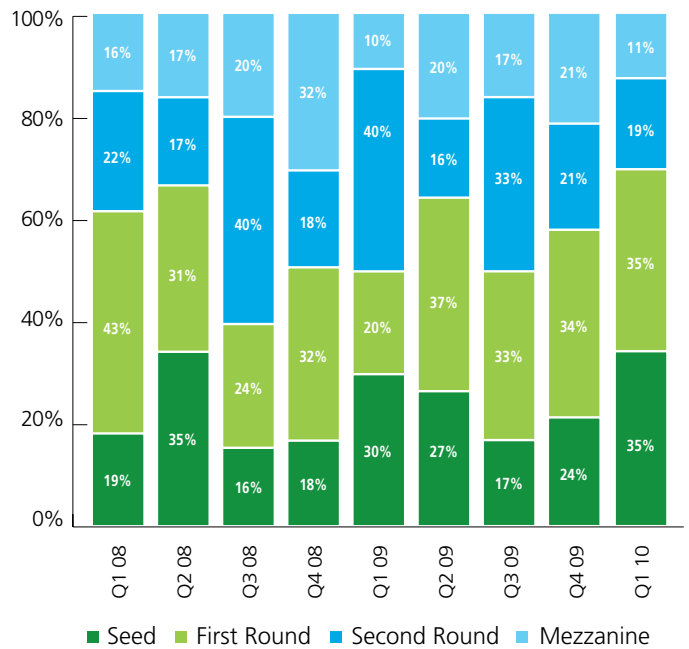
main gap is in the Seed Stage, 32% in the First Round, 25% in the Second Round, and 16% in the Mezzanine Stage. It is interesting to note that there is a clear shift in the investment gap focused on earlier stages with only 16% of respondents forecasting an investment gap in the start-up industry compared to 35% in the preceding quarter. Seed and First Round, as an aggregate contributed to 60% of ventured capitalists presumed investment gap in Q1, 2010 compared to 53% in Q4, 2009.

Chart 4: What is the main investment gap in the Israeli start-up industry?



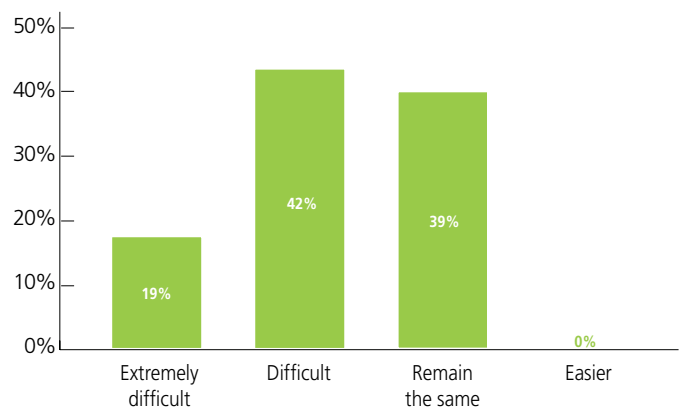
The segmentation of forecasted new investments reflects an increase in terms of optimism in comparison to previous quarters. Such that 35% of respondents expect to focus a majority of their new investments in Seed Stage, equivalent to a jump of 11%, in comparison to the previous quarter. 35% expect the majority of new investments to be made in First Round, and the remaining 30% of respondents, expect to invest in later stages. Early investments (Seed and First Round) are beginning to reflect trends that controlled the venture capital industry before the "Credit Crisis". As can be seen in the end of 2007 and the beginning of 2008, where there was a much higher tendency to invest in earlier stages. The evident up leg seems to provide a clear indication that we are returning to pre-crisis levels.

Chart 5: During the next six months, I expect the majority of my new investments to be made in:



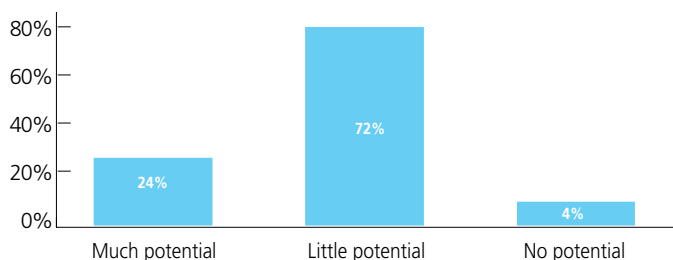
Despite much optimism in terms of most factors affecting venture capitalists, an imposing 61% of respondents claim that fundraising will become more difficult. 38% of surveyed participants claim that it will remain the same, while in parallel no venture capitalist believe that fundraising will become easier. What is more daunting is that these figures bear much resemblance to last quarter's pessimism regarding fundraising activity.

Chart 6: VC Fundraising activity will become:



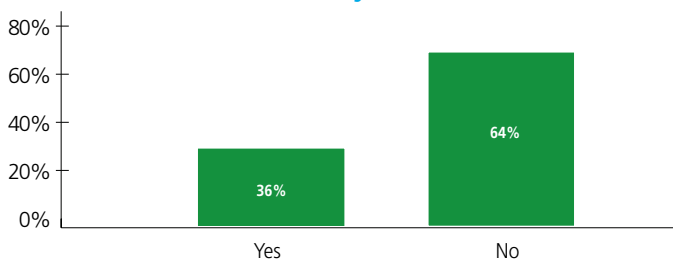
The recent announcement of launching a new venture capital fund that will operate in the Israeli-Arab community, the third Israeli VC to do so, is an inspiring example that corresponds with our data where 96% of respondents forecast the Arab-Israeli technology market to have potential.

Chart 7: Do you believe that the Arab-Israeli technology market has _____ ?



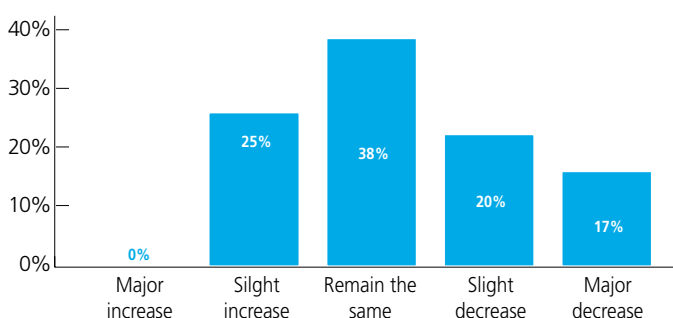
Despite a vast majority of respondents forecasting the Arab-Israeli technology market to hold potential, only 36% of respondents believe collaboration between Israel and Arab technology companies will exist within the year.

Chart 8: Do you believe that Arab technology companies and Israeli technology companies will collaborate within the next year?



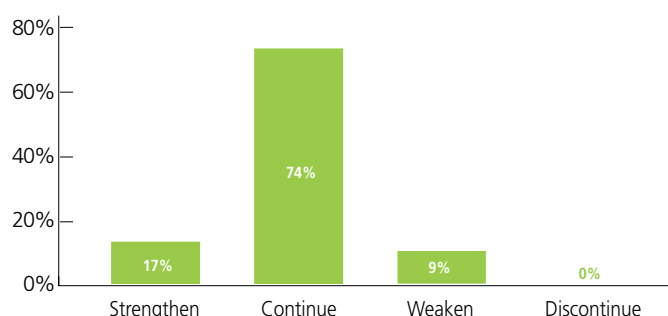
Projected fund size in terms of AUM doesn't express the same optimism shared in much of the other issues reflecting venture capital sentiment. Whereby, zero respondents believe a major increase will exist and only a quarter forecast a slight increase. 38% of respondent's expect the projected fund compared to the current fund to remain the same, followed by over a third claiming a decrease in fund size.

Chart 9: Projected fund size compared to current fund size (by AUM):



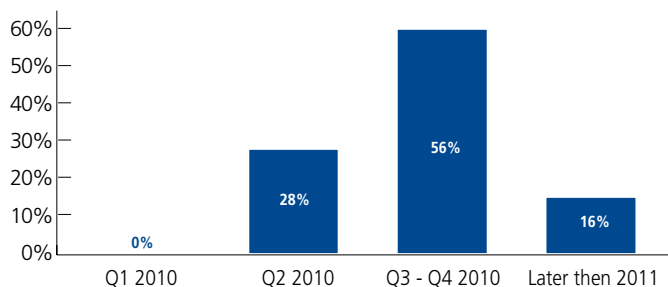
The sudden emergence in Life Science IPOs on the TASE bears little surprise to why 91% of respondents forecast this hype to continue, whilst no respondents believe this trend to discontinue.

Chart 10: Recent hype on the Tel Aviv Stock Exchange (TASE) in the Medical Device and Life Science sectors will _____ :



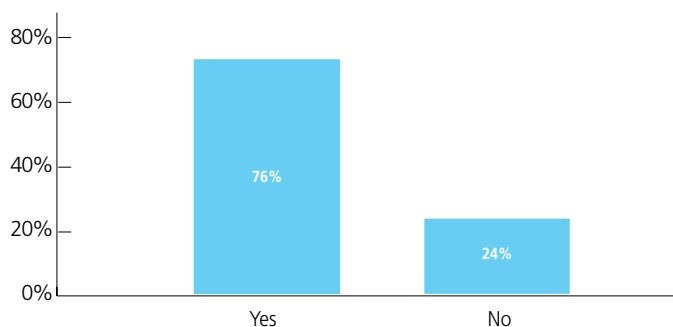
Optimism seems to be creeping in, with a significant majority of 84% of respondents claiming that the next IPO on the NASDAQ will be held by yearend. It is essential to note that Israel has not contributed to any IPOs on the NASDAQ since July, 2007 (Voltaire) and the probability for such an event being imminent seems to be increasing exponentially as sentiment continues to pick up. An inspiring jump since the previous quarter of 34% of respondents forecast Q3 - Q4, 2010 to be the quarter which embarks Israel's first IPO since 2007, indicates that venture capitalists are seeing more light at the end of the tunnel.

Chart 11: When do you believe we'll see the next Israeli IPO on the NASDAQ?



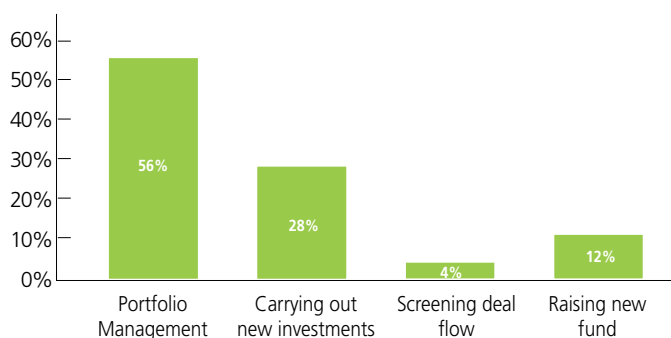
Despite a significant 76% of surveyed participants claiming that M&A transactions are ramping up, this result is 15% lower than Q4, 2009. Even though this reflects a setback for M&A sentiment amongst venture capitalist, it clearly reflects the apparent turnaround since the inception of market turmoil.

Chart 12: I believe M&A transactions are ramping up?



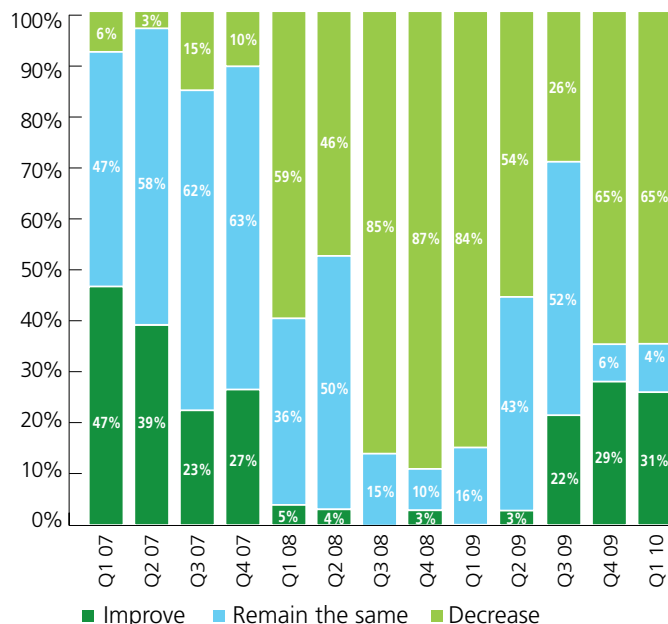
According to venture capitalists, 56% of them expect to allocate a majority of their time to Portfolio Management a 9% decrease since Q4, 2009. Despite increased optimism, perpetual instability sheds clear indication to why only 20% of venture capitalist's time is expected to be spent on carrying out new investments. On the flipside, 12% of respondents expect to spend the majority of their time focusing on raising a new fund compared to only 3% in Q4, 2009.

Chart 13: During the next three months, I expect to spend the majority of my time focusing on:



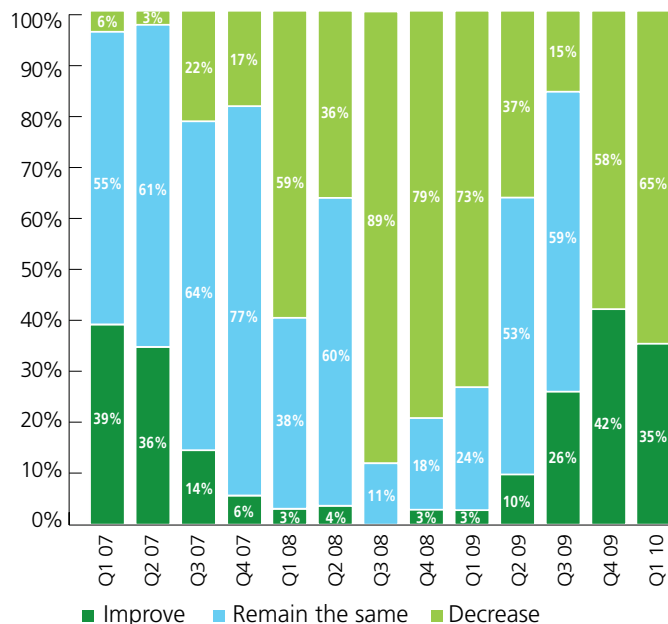
In terms of today's growing positive sentiment, investment valuations paint a more distorted picture. Such that, expectations are poised for higher valuations by 2% (QoQ) of respondents and increases have been climbing every quarter since Q1, 2009. However, a whopping 65% of venture capitalists continue to expect decreases in valuations, whereas only 4% assert valuations to remain unchanged.

Chart 14: During the next six months, I expect investment valuations to:



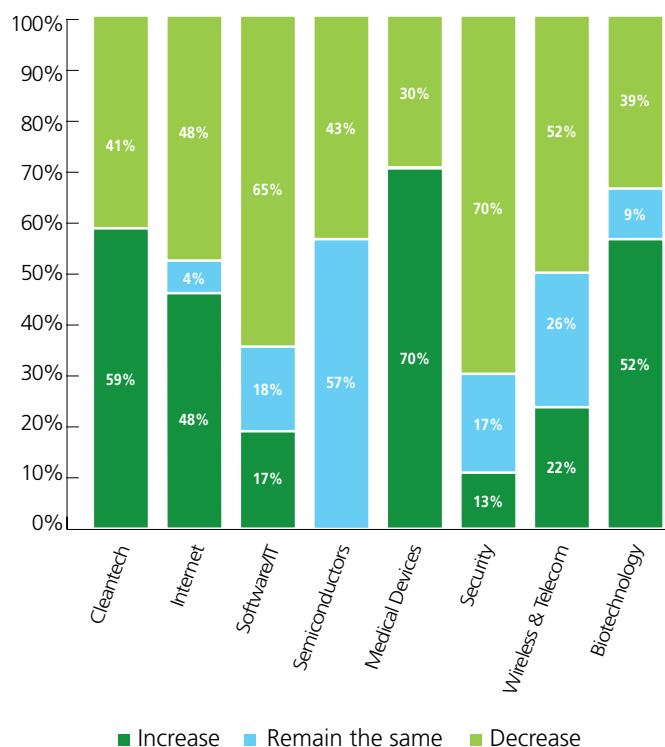
Exit valuations provide similar signs of a collage of mixed optimism and pessimism. The evident divergence in exit valuations conveys some confusion to where venture capitalists feel we are headed in terms of exit valuations during the next six months. However, a clear improvement in exit valuation expectations is expressed through 65% forecasting decreases in valuations in the next six months, comparing to 73% in Q1, 2009. However, a noteworthy 35% claim improvements are around the corner, comparing to a frightening low of 3% in Q1, 2009.

Chart 15: During the next six months, I expect exit valuations to:



In concurrence with the new found hype in the Life Science sector, expectations for transaction growth in the Medical Device industry have grown immensely. 70% of respondents claim that Medical Devices will project the highest number of transactions during the next six months. A continuation of improvements in terms of transactions was also evident in the Biotechnology and Internet sectors (52% and 48%, respectively). According to respondents, there is a 13% drop in terms of the number of transaction expectations in the Cleantech sector which is the first drop since the financial crisis began. Not surprisingly, the Semiconductor sector is forecasted to demonstrate the sharpest decline in transactions which has been a consistent notion for the past several quarters.

Chart 16: During the next six months, I expect the number of transactions in the sectors listed below to:



Insights

The continued improvement in venture capital sentiment in Israel seems to be gaining momentum when comparing Q1, 2010 to previous quarters. Despite some degree of suspicion still evident, the general perception amongst respondents indicates increasing improvement in market perceptions. This trend, which has been gaining traction since the end of Q1, 2009 has been rising steadily with surveyed data reflecting improving economic climate amongst 58% of respondents, in comparison to a staggering low of 0% in Q1, 2009.

Early investments (Seed and First Round) are beginning to reflect trends that controlled the venture capital industry before the "Credit Crisis". As can be seen in the end of 2007 and the beginning of 2008, where there was a much higher tendency to invest in earlier stages. The evident up leg seems to provide yet another clear indication that we are returning to pre-crisis levels. Additional signs of optimism were shed through a significant 76% of surveyed participants claiming that M&A transactions are ramping up which clearly reflects the apparent turnaround since the inception of market turmoil.

The expectations of Israel embarking on its first IPO on the NASDAQ seem to be creeping in, with an impressive 84% of respondents forecasting 2010 to unfold as Israel's first IPO since 2007. Venture capital optimism can be expected to continue to strengthen but it is essential to note that much of this positive sentiment has been associated with the sudden emergence in Life Science IPOs on the TASE, whereby 91% of respondents forecast this hype to continue.

In concurrence with the new found hype in the Life Science sector, expectations for transaction growth in the Medical Device industry have grown immensely. 70% of respondents claim that Medical Devices will project the highest number of transactions during the next six months. A continuation of improvements in terms of transactions was also evident in the Biotechnology and Internet sectors (52% and 48%, respectively). With such prevalence of optimism it was interesting to witness the lowest levels of confidence in the Semiconductor sector since Deloitte Brightman Almagor Zoar began surveying venture capital sentiment in Israel.

March 2010's addition of a new venture capital fund (Al-Bawadir Fund) that will operate in the Israeli-Arab community is an inspiring example that corresponds with our data where 96% of respondents forecast the Arab-Israeli technology market to have potential. In spite of optimism pertaining to the potential of this market, only 36% of respondents believe collaboration between Israel and Arab technology companies will exist in the very near future. Now the question remains "will this new fund built on such a fragile alliance manage to prevail"?

Contacts

We welcome suggestions for issues to be addressed in future Israel VC Indicator Surveys. You are welcome to send your suggestions to Rony More at romore@deloitte.co.il

Please contact us for further information about the results of this survey, the special services offered by Deloitte Brightman Almagor Zohar and its affiliates to VCs, and assistance with deal initiation and the execution process.

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