

ISRAEL HIGH-TECH & INVESTMENT REPORT

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“Follow the leader”



In less than half a year, Warren Buffett's purchase of 80% of Israel's Iscar Ltd. for \$4.0 billion has become a veritable legend. The deal began with an ordinary e-mail from Eitan, the son of Steff Wertheimer, the company's

founder. Eitan stated that Iscar was up for sale. The initial contact, which led to the sale, became the single largest investment into an operating Israeli company. Warren Buffett first visited Israel and Iscar, after the deal was concluded. In retrospect Iscar's corporate profile is typical of many of the Buffett investee companies. Iscar is a family owned company that is fully devoted to its business affairs and has a history of many years of profitability and growth in sales.

Warren Buffett is considered one of the world's canniest investors. Since the purchase he has expressed total satisfaction and called it “a winning bet”.

We recently came across a table of two years of merger and acquisition activity in Israel. In this issue we are reproducing the table that lists the merger & acquisition activity by sector, sum invested and date.

In 2005 the merger & acquisition activity totaled \$3.4 billion. In 2006 the M & A activity, prior to the date of the announcement of Warren Buffett's investment totaled \$616m. The “post-Buffett” investment activity totaled \$10.4 billion. About half of this was accounted for by two companies, whose decision making process behind these massive deals, was totally unrelated to that of Warren Buffett.

Yet, though there is no way to absolutely prove the point, this other half of the total M & A activity in 2006 was most likely favorably influenced by Warren Buffett's stamp of approval of Israel.

We believe that 2007 will prove to be another banner year for Merger & Acquisition activity, with so many new entrants appearing on the scene.

The maturing start-ups are attractive to foreign investors. A case in point is the most recent acquisition by of iRows, which Google has acquired for an undisclosed sum of money. The acquisition is intended to improve Google's existing spreadsheet services. iRows has created online spreadsheet allowing the user to access its spreadsheets online from anywhere.

Israeli companies, once priced at discount to the global market, are beginning to achieve premium valuations.

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World Bank ranked Israel 5th best for investor protection

Swiss pharma giant expands activities in Israel

Unconventional but Orthodox

New Zealand navy plans to buy Israeli anti-terror guns



The New Zealand Navy plans to buy sophisticated new Israeli-made automatic gun systems to protect its frigates from the threat posed by terrorists using explosive-laden speedboats.

The latest issue of the navy's monthly magazine Navy Today reports the Rafael mini-typhoon gun direction system is being procured for the Anzac-class frigates.

The system uses a sophisticated camera and a laser range-finder to automatically aim a stabilized machine gun at any likely threat. The gun is controlled from a ship's operations room but it can also be set to fire independently.

Israelis have fitted similar guns to unmanned high-speed patrol craft and the Australian navy is fitting it to its new patrol craft.

Allot IPO exceeds expectations



IP service optimization solutions developer Allot Communications Ltd. successfully held the pricing stage of its IPO on Nasdaq. It is the

second Israeli high-tech company to go public on Wall Street within a month. RR Satellite Communications Ltd. (Nasdaq:RRST) recently held its IPO.

The company raised \$78 million, at a share price above the target range.

Allot issued 6.5 million shares, 27% of its share capital, at \$12 per share. The target range for the IPO was \$9-11. The issue price gives Allot a company value of \$293 million, above the projected value of \$188-230 million.

Allot plans to use the proceeds of the offering for regular operations and R&D.

The company will be traded under the ticker "ALLT".

The IPO marks a successful exit for five Israeli venture capital funds that invested in Allot: Gemini Israel Funds, Genesis Partners, Partech International, Jerusalem Venture Partners (JVP), and Tamir Fishman Venture Capital (TASE: TFVC).

Intel's Israel-developed "Quad-Core Processor" enters the market

Intel, the world's largest maker of computer processors, announced that its new quad-core microprocessor was ready for the market.



Developed at Intel's research and development center in the northern Israel port city of Haifa, the quad-core technology was not supposed to be ready until mid-2007.

Hailed as a "four-brain" computer, Intel President and CEO Paul Otellini said that the new processor "ushers in another new era in computing. The capabilities of quad-core microprocessors will bring new possibilities for science, entertainment and business."

The quad-core works by combining four computing microprocessors inside a single chip, greatly increasing processor speeds and helping to save on energy.

Intel's Haifa center was responsible for originally introducing the multi-core microprocessor concept, which the company says has given it a new edge over competitors.

Intel Corp. has announced the opening in of a multicore processor technology laboratory in Haifa, Israel. The laboratory is to develop and run tests to allow independent software vendors (ISVs) to benchmark their applications on the Intel processors.

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The announcement was made at the Intel Developer Forum recently held in Tel-Aviv. At the event Intel also demonstrated the use of its processors for graphical processing for the film industry. According to the presentations, film can be completely replaced by direct capture to disk with the processing at each stage done with Intel architecture platforms.

Telecom Israel 2006

Telecom Israel 2006, Israel's 8th Telecom Exhibition was recently held in Tel Aviv. Telecom 2006 featured innovations and explored the professional aspects of telecommunications, cellular technology, IT security, infrastructure, applications and Internet content. The Exhibition, which served as the kick-off for ITU Telecom World 2006 in Hong Kong, to be held on December offered many Israeli companies an opportunity to conduct a professional 'rehearsal', prior to their opening the show in Asia as well as facilities for forging preliminary ties with foreign business delegations.



Yechiel Assia, Director General of the Israel Export and International Cooperation Institute estimated that over 300 meetings were held with Export Institute managers. Hundreds of additional business meetings took place between potential, interested buyers and presenting companies, manufacturers and developers of advanced technologies.

The exhibition was visited by 25 foreign delegation from eighty countries as well as 20 Ministers and Deputy Ministers of Communication who arrived in order to learn about the Israeli telecom industry and discover how Israel succeeds in exporting so extensively considering its limited size and population, and how it achieved its leading position in so many areas of this industry.

Telecom Israel 2006 also hosted over 50 of the world's leading media organizations, including those located in target countries for Israel's telecommunications export.

Israel exports over one billion dollars worth of telecommunications to North America; over \$825 million worth to the EU and \$720 million to Asia. Yechiel Assia reported that the most impressive increases in export are to two destinations: China and India.

Dutch Air Force chooses Rafael Litening targeting pod

The Royal Netherlands Air Force (RNAF) will fit its F-16 fighter aircraft with Litening targeting pods made by Rafael Armament Development Authority Ltd. and Northrop Grumman (NYSE: NOC). Under the deal, which is worth an estimated \$40 million, the RNAF will purchase 20 Litening pods plus support equipment for ground and aircrews.

The Litening is one of the world's most advanced attack and navigation pods. It is equipped with day and night vision capabilities, enabling detection, recognition, identification and laser designation of air-to-surface and maritime targets, enabling the delivery of laser and GPS-guided munitions.

Rafael said that the deal with the RNAF underscored the Litening's position as the world's leading assault and navigation pod. The spokesman added that the RNAF also purchased Rafael's Reccelite Tactical Reconnaissance pods several months ago.

More than 700 Litening pods are now in use in the air forces of the US, Australia, Hungary, and Israel Air Force's F-16 fighter, as well as on the German Luftwaffe's Tornado fighter aircraft. The Litening is also being integrated into the new EuroFighter Typhoon aircraft.

Rafael and Northrop Gruman will begin deliveries of the pods in 2007, with the procurement due to be completed in 2008.

"Believe in Israel - Fortify the Ties"

Presentation By British Ambassador Tom Phillips at the Prime Minister's Conference on Export and International Co-operation, Tel-Aviv.



"I should like to cover both the nature of the business and economic links between my country and Israel, as an illustration of a healthy partnership between two countries with a similar view of the opportunities provided by globalization, and some thoughts on the interplay between political processes and trading links in this part of the world.

And our two countries have done so. In a difficult year, two-way trade has increased by 6%, two-way investment is increasing, with over 200 local companies having a base in Britain, and major British companies such as HSBC, APAX, British Airways and British Gas having significant interests in Israel. A4e/Amin are making a notable difference through their involvement in the ambitious Wisconsin Project, which aims to integrate welfare recipients into the workforce.

Britain has over one trillion pounds of investment stock, making it second only to the USA in terms of FDI. The reason for its success in attracting investment is because of our macro-economic stability, a skilled workforce, our rates of enterprise and the light nature of the UK regulatory framework.

Israeli companies continue to raise capital on the LSE/ AIM markets: 25% of all international listings on AIM last year were from Israel. London now has a 26.4% share of the global IPO market compared to just 6.5% in New York. Britain is a natural choice for Israeli companies: the English language, Britain's physical and political position in Europe, excellent transportation links, the fact that Britain is less than 5 hours away by plane and just a two hour time difference – all mean that it is easy to do business with Britain and from Britain.

The news about the investment climate in Israel is also good. A recent survey in The Economist magazine predicted record high foreign direct investment in Israel in 2006 – upwards of \$9 billion. This would put Israel in 10th place for FDI among 27 emerging markets. People invest here because Israel has a market-based economy, lots of entrepreneurial spirit, a legal system based I'm proud to say on British law, and good international connections.

I find it interesting that our two economies, and our two business communities, have developed such similar enterprise climates, and indeed I see the business link between our two countries as an example of how even in a globalized economy a strong bilateral relationship between countries and business people in those two countries can work to mutual advantage.

In the high-tech arena growth has been astronomical: output has trebled in pharmaceuticals and doubled in aerospace. Some manufacturing jobs have been lost, but 2.3 million more jobs have been created in the British economy as a whole since 1997.

This parallels what has happened here. I note that the recent World Economic Forum report ranked Israel in 15th place on competitiveness (a terrific improvement over last year's 23rd place, although I am patriotically glad that Britain came in a little bit higher, at Number 10).

Israel's particular strengths were noted as:

- * technological readiness (3rd in the world)
- * improvements in macro-economic management, and
- * improvements in market efficiency and infrastructure.

But I would also like to end by noting how much brighter the picture could be were Israel's place in the region to be secured by further peace agreements, taking the country out of as much as possible of the 'shadow of confrontation' mentioned in the title to this session.

Although Israel's businessmen rightly look further afield than the region, history nevertheless suggests that there can be very real gains for Israel in finding peace with its neighbors. Israel's relations with her neighbors have delivered real benefits. Annual trade between Israel and Jordan rose ten-fold to \$130 million between 1996 and 2003. Israeli exports to Jordan rose to over \$100m in 2004. 150,000 Israeli tourists visit Jordan each year. And nearly 400,000 Israelis visited Egypt in 2004.

This may pale in comparison to Israel's commercial relations with the EU and US. But the potential is there. By working with her neighbors, Israel can find joint solutions to the economic, environmental and security problems, which she faces in the region".

Network Appliance buying Topio

Network Appliance (NASDAQ: NTAP) announced the acquisition of Topio for \$160 million cash.



The deal, expected to close in December, is Neap's first acquisition outside the U.S., and the first in Israel.

To date Topio has raised \$20.5 million. One of its backers is Sequoia Israel, which put in \$8 million and owns approximately one-third of the company.

The acquisition also makes entrepreneur Yoram Novick a millionaire.

Topio, which operates out of in Santa Clara, California, will maintain its R&D center in Haifa and will turn into a business division of NetApp.

Novick founded Topio in 2001. The company developed software-enabling clients to copy, recover and safeguard data at any distance, irrespective of their server or storage platforms. The combination of Topio's software with NetApp's data management software will enable enterprises to replicate production data from the suppliers' systems, including HP, EMC or HDS, to any NetApp storage system, without disrupting working processes.

The average enterprise creates and stores anywhere between 10 and 20 copies of its data, including testing and application development data, which can increase the amount of storage consumed by ten to 20 times.

Sequoia Israel managing partner Shmil Levy commented that when the Topio people first showed up, all they had in hand was an idea and some slides. "They had no experience in startups, but we saw very talented guys with a great vision," he relates.

AOL acquires Relegence for rumored \$50-\$100 million

The acquisition, whose price was not released, helps to define what's increasingly called a new attention-based economy. The conventional wisdom of this model rewards companies such as Relegence for helping users decide what to pay attention to in an exploding universe of digital media content.

With Relegence, AOL gets a company that sells subscription-based services that offer real-time discovery, notification and delivery of information to connecting customers with cross-media content as it is generated from anywhere across the globe.

Relegence simultaneously monitors, indexes, and filters more than 20,000 unique, global sources of live content streams.

The streams include local and international newswires, print media, television and cable networks, regulatory feeds, corporate and information web sites, internet bulletin boards.

AOL said Relegence's proprietary technology then delivers to a user's desktop only the information relevant to his or her individual search criteria.

In an age of constant content production from countless media sources, that's a pretty handy trick. And it's one AOL was willing to pay to learn.

AOL said the acquisition will help it better serve public and enterprise users with a comprehensive and timely content experience.

But AOL isn't the only company to bet that users will see value in being served only the most relevant content.

In fact, AOL is only one player in a growing attention-based economy, where a constant stream of content has led to demand for the kind of parsing companies such as Relegence supply.

Last summer, The New York Times began experimenting with a product called My Times for its NYTimes.com property. The product's main features are syndication feeds it opens to subscribers, which are stuffed with content selected by New York Times editors and writers.

The division of worthwhile and best-ignored on the Web is also the main service proved by sites such as Digg.com, del.icio.us, and even AOL's revamped Netscape.com.

For now, AOL said that Relegence will act as a wholly-owned subsidiary and will continue to partner with financial services firms. The new property and its 60 employees will continue to be headquartered in New York, with offices in London and Tel Aviv.

Wintegra is Israel's fastest growing tech company

Deloitte Touche Brightman and Almagor presented this year's fastest growing Israeli technology company award to Wintegra, a developer of semiconductors that achieved a phenomenal growth rate in sales from 2001 to 2005.



The Fast 50 Israel is part of a Deloitte worldwide Fast 500. It identifies the 500 fastest growing technology

companies in the world.
Israel's first Fast 50 contest took place in 2000.

This year's runner up in the Fast 50 was Syneron Medical, which achieved an accelerated growth rate during those five years. The company develops non-surgical medical aesthetics equipment. Third place was taken by Runcom, which also achieved a rapid growth rate during those five years. The company develops technologies for G3 mobile phones

Ormat Technologies beats forecast for Q3 with \$78m sales

Ormat Industries (TASE: ORMT) subsidiary Ormat Technologies (NYSE: ORA) filed fine third-quarter financials today, beating revenue forecasts and meeting predicted earnings.

The green energy company said total third-quarter revenues were \$77.8 million, up 12% from \$69.3 million in the same quarter in 2005. Sales beat the forecast on Wall Street by half a million dollars.

Ormat, which builds and operates geothermal and other 'alternative' power stations, netted \$13.9 million or \$0.39 per share. In the parallel 2005 quarter it netted \$12.3 million or \$0.39 per share.

Electricity Segment revenues for the quarter were \$56.4 million compared to \$51.4 million for the same quarter in 2005, an increase of 9.8%.

The increase in revenues was primarily attributed to a growth in generating capacity, which increased the company's revenues by \$1.3 million, Ormat said. It also included a full quarter of \$3.5 million in revenues generated from the Zunil geothermal project in Guatemala, which was consolidated as of March 13, 2006.

Ormat's gross margin narrowed to 41.6% of turnover, versus 45.3% the year before. Gross margin was impacted by a reduction in Electricity Segment margins, which were lower due to the repair cost of the Puna wells and an increase in the operating costs, some of which were related to new power plants that came on line during the quarter but did not yet contribute fully to revenues.

Operating income for the third quarter was \$24.9 million, down from \$25.3 million for the same quarter in 2005.

Nine-month revenue rose 13% to \$202.3 million, on which Ormat netted \$30.2 million or \$0.89 per share. In the nine-month period of 2005, it netted \$20.3 million or \$0.64 per share.

USAF to purchase 20 Python 5 missiles

US defense news magazine "Defense News" reports that the US Air Force is to buy 20 Python 5 Full Sphere air-to-air missiles from Rafael Armament Development Authority Ltd., for a F-16 fighter squadron stationed at Nevada. Should the negotiations lead to a contract, this will be the first time that the US Air Force has purchased air-to-air missiles from a foreign manufacturer. Sources at Rafael's US office declined to comment on the



report.

"Air-to-air missiles are a matter of masculinity, like fighter aircraft or tanks. Missiles like these are the kind of weapon that fighting organizations find difficult to buy from a foreign party since they represent the core of their being," said former Pentagon official Frank Cevasco, who managed international development and production programs under four US defense secretaries.

Over the years, the Pentagon has purchased from foreign manufacturers, air-to-surface missiles for fighter aircraft in the US Air Force and Navy. Also included among the purchases were AGM-142 (Popeye) missiles from Israel, Durandal missiles from France, and Penguin missiles from Norway. However Cevasco and other procurement specialists at the Pentagon could not recall a single case where the US Air Force purchased air-to-air missiles from a foreign company.

Magna BSP wins €320m French radar contract

Magna BSP of Dimona, Israel has won a contract to supply radar systems for the French military's perimeter defense plan. Magna CEO Haim Siboni said that following the win in the competition, the company expects orders from the French military of up to €320 million over five years.



The trials took place at a French military base in Orleans in recent weeks under the supervision of the French Department of Defense and French consortium Thales, which is the French military's chief contractor on its perimeter defense project.

The competition, in which 15 leading radar systems companies from around the world took part, included day and night trials using hundreds of intrusion scenarios for open spaces, houses and agricultural companies. The Israeli radar system won first place after it detected all of the intrusion attempts in a series of tests without a single false alarm.

Siboni said that during the trials Thales representatives gave the intruders GPS units in order to test the precision of the radar systems' identification, and the Israeli system scored the highest marks of all. In the final part of the trials, a dog was let into the test site to see whether the radar systems could distinguish between the dog and the intruders. The Israeli system was the only one that successfully did so.

Teva Q3 profit up on generic sales

Teva Pharmaceutical Industries Ltd. (NASDAQ: TEVA) reported that third-quarter earnings rose on strong sales of generic versions of blockbuster treatments for depression and cholesterol, as well as its recent acquisition of Ivax.



Net income at the Israel-based company rose to \$606 million, or 74 cents per share, from \$267 million, or 40 cents per share, a year earlier, it said on Tuesday.

Sales for the third quarter rose 74 percent to \$2.29 billion.

Teva President and Chief Executive Israel Makov said the company had a strong launch of Azilect, its innovative treatment for Parkinson's disease. The drug was launched in the United States in July and is available in 22 countries.

He also said Teva was realizing "tremendous synergies" from its acquisition of IVAX, completed in January.

North American drug sales reached \$1.325 billion in the quarter, up 87 percent from a year earlier.

Sales benefited from 22 new products that were not sold in the 2005-quarter, including simvastatin and pravastatin for lowering cholesterol and sertraline for depression.

Teva has 144 product applications awaiting final

approval from the U.S. Food and Drug Administration. The brand products covered by these applications have annual U.S. sales of \$87 billion.

The company has announced that global market sales of its drug Copaxone for the treatment of multiple sclerosis increased 15% to a record \$354 million in the third quarter of 2006.

In the US Copaxone continues to outpace the market growth with total prescription share increasing to 34% and new prescription share increasing to 35.2%, as of September 2006. US sales in the third quarter of 2006 increased 10% over the third quarter of 2005 to \$226 million.

Teva added that outside the US, mainly in Europe, Copaxone was the fastest growing MS therapy with growth of 26% over the third quarter of 2005, reaching sales of \$128 million.

Copaxone is now a 'blockbuster' drug, with annual sales in excess of \$1 billion.

Teva also said its board authorized the company to repurchase up to \$600 million of its ordinary shares/ADRs and convertible debentures of its finance subsidiaries.

The repurchase program is Teva's third in recent years.

Solel allying with Spanish firm in giant \$900 million solar power project

Beit Shemesh Israel -based Solel and the Spanish infrastructures company Sacyr Vallehermoso are teaming up to handle Euro 700 million (\$890 million) worth of solar energy projects over four years.



Sacyr Vallehermoso specializes in producing electricity from renewable sources. It and Solel, which specializes in building solar energy power stations, will be founding a joint company (50-50) that will start by building three power stations, each producing 50 megawatts.

Solel's part of the project is about half a billion dollars.

This is the first time that the company from Beit Shemesh has been tapped to carry out a turnkey project, serving as direct manufacturer and supplier of clean power in Europe, and not only a supplier of

thermo-solar energy systems.

The stations should sell the power they make to Spain's national power company, for 30 cents per kilowatt/hour. The Spanish government is subsidizing the price, in order to encourage solar power production.

Industry sources project that Solel will be selling \$500 million worth of equipment to the joint company by the end of 2008, making it one of the biggest "green energy" companies in Israel, alongside Ormat Industries (TASE: ORMT) .

Telecommunications equipment exports will be \$3.3 billion this year

Telecommunications equipment exports are expected to advance 14% in 2006 to \$3.3 billion, according to Export Institute head Yechiel Assia.

Based on that projection, telecommunications would be responsible for 20% of Israel's technology exports this year.

Export of telecommunications gear to North America is believed to have grown by 8% this year to about a billion dollars, while exports of the equipment to the European Union increased by 18% to \$825 million.

Exports of telecommunications equipment to Asia increased by about 25% to \$720 million, he predicts.

GD licenses Thor bomb-disposal system

A General Dynamics unit, has signed a licensing agreement with an Israeli company for its Thor ordnance disposal system.

Thor combines a high-tech laser and an old-fashioned machine gun that combat engineers and EOD teams can use to destroy explosive devices in the field from a safe distance.

The deal between GD's Ordnance and Tactical Systems unit in Florida and RAFAEL will result in the Thor system being made available to U.S. customers. It was not immediately known if the U.S. military had any immediate plans to acquire Thor.

The 700-watt laser produces a burn, that consumes the explosives inside the device without causing an explosion and knocks out unexploded ordnance and roadside bombs.

"Thor has demonstrated combat effectiveness in operational engagements bringing an additional precision-fire gun platform to the fight, while at the same time filling a unique tactical mission role," pointed out GD Vice President Richard Davitt.

Thor can be mounted on a variety of manned and unmanned vehicles and includes day and night-vision sighting sensors. The 250-pound unit rests on a stabilizing platform that allows precision shots from both the 50 weapon and the laser.

NICE reports 78% rise in profit

Nice Systems (NASDAQ: NICE) reported a quarter, in which it managed to beat analyst' expectations.

Revenues reached a record \$112.2 million in the third quarter of 2005, an increase of almost 36% compared with \$82.7 million in the same period of 2005.

Non-GAAP profit was also a record at \$16 million or 31 cents per share, an increase of 78.5% from the year before.

Operating income also reached unprecedented levels, rising to 16% of turnover or \$17.8 million, compared with 11% of turnover or \$9.5 million in the third quarter of 2005.

CEO Haim Shani commented that the results demonstrate the successful execution of the company's long-term plans and rising demand for the company's solutions, in both the enterprise and security markets.

Nice also raised its forecasts for the year and said it expects fourth-quarter 2006 revenues in the range of \$115-120 million, and non-GAAP EPS of 32-37 cents. For the year the company expects sales of \$413-318 million, while previously it had guided investors to expect sales of \$408-417 million.

7% of Israeli VCs see rise in "cleantech" investment

Deloitte Brightman Almagor's survey finds that 55% of venture capital managers believe that the number of transaction in Internet will rise.

The current buzzword in Israeli venture capital is cleantech, states Deloitte Brightman Almagor in its "Israel VC Indicator Survey" for the third quarter of 2006. The survey is conducted among Israeli venture capital managers.

67% of respondents expect to see an increase in investment transactions in cleantech, far higher than other sectors during the next six months. In second place, 55% of respondents believe that the number of transactions in the Internet sector will increase.

Deloitte Brightman Almagor chairman and CEO Yigal Brightman said, "Cleantech is attracting more interest. It's not just talk; money is beginning to flow to investment in the field. That said, it seems that the venture capital industry is still only in the initial stages of learning about the field. I believe that there's a need for a strong tie-in with academic institutions where it's possible to be exposed to a large number of technological opportunities in the field."

Cleantech includes services, products and processes designed to produce various results at lower cost and higher quality, while minimally affecting the environment. Cleantech is broken down into a number of subsectors, including water desalination, clean energy production, and materials manufacturing technologies. Topios include geothermal energy, solar energy, water purification, and biological desalination.

Commenting on the Internet sector, Brightman said, "In view of the giant YouTube deal, we can assume that Internet will continue to grow. In the quarterly VC Indicator Survey of six months ago, we saw growing interest in the Internet. Companies that survived the last bubble and demonstrated that profitable business models can achieve significant growth in the Internet. Those choosing the right model can create immense value for shareholders."

The current survey found that, despite high-tech stamina, venture capital managers are less optimistic about the Israeli economic climate. 37% predict that the economic climate will improve over the next six months, down from an average of 55% in the last three years.

Furthermore, 15% of venture capital managers predict that Israel's economic climate will decline over the next six months, compared with 11% in the previous quarter. 48% believe that the economic climate will remain unchanged, up from 42% in the previous quarter.

As for the second Lebanon war and its impact on the Israeli economy, venture capital managers are

signaling "business as usual". The war did not affect Israeli high-tech, or the venture capital industry. The survey found that the war had little or no effect on these sectors.

As for the war's impact on foreign investment, 52% of respondents believe that foreign investment in venture capital funds will decline slightly, 44% believe the war will have no effect, and 4% believe that foreign investment will increase.

Brightman said, "Although foreign investors are closely reviewing the risk of escalation in the Middle East, they still assume that in the long term, Israel's economy is strong and that its competitive advantage in high-tech will be maintained. We can assume that so long as no major escalation develops, and international intervention to calm things down in the area continues, foreign investors will continue to channel resources to Israel."

The survey found that IPOs will be a secondary exit strategy for most high-tech companies. 33% of venture capital managers believe that exit valuations will improve, down from 55% in the first quarter of 2006 and 55% in the fourth quarter of 2005.

Israeli High-Tech Company Capital Raising Q1-Q3/2006

In the third quarter of 2006, 87 Israeli high-tech companies raised \$381 million from venture investors – both local and foreign. The quarterly amount was down 6 percent from the \$404 million raised in the previous quarter, but was 13 percent above the \$336 million raised in the third quarter of 2005.

"The small decrease in investment in Q3 indicated that the war, which took place during the third quarter, had only a very minor impact on venture capital investments," said Zeev Holtzman, Chairman of both IVC Research Center and Giza Venture Capital. "It signifies that investors continue to see stability and credibility in Israeli high-tech, a fact which is also reflected in the slight increase in the share of foreign investment during the Q3 period."

The first nine months of 2006 showed a 7 percent increase in capital raising to \$1.145 billion, compared to \$1.073 billion in the corresponding period in 2005,

Israeli VC Investment Activity

In Q3, Israeli VCs invested \$142 million in Israeli companies, compared with \$154 million invested in

the previous quarter and \$188 million in Q3 2005. The Israeli VC share of the total amount invested in Israeli high-tech was 38 percent, with the remainder of capital coming from foreign investors as well as non-VC Israeli investors.

First investments accounted for 44 percent of total dollar investments by Israeli VCs in the third quarter, compared with 35 percent in the previous quarter and 41 percent in the third quarter of 2005. The average First investment by Israeli VCs was \$2.25 million, while the average Follow-on investment was \$0.85 million.

In the first three quarters of 2006, the Israeli VC fund share of investments in Israeli high-tech companies was 41 percent, compared to 49 percent in the corresponding period in 2005. The share of foreign investors as well as non-VC Israeli investors increased, therefore, to 59 percent from 51 percent.

First investments by Israeli VC funds were 37 percent of their total investments, versus 44 percent in the corresponding period in 2005.

Check Point buying Sweden's Protect Data for \$586 million

The Israeli data security company Check Point Software Technologies (Nasdaq:CHKP) said it would buy data security company Protect Data (Stockholm:PROT.ST) for about \$586 million.

This is just the second acquisition in Check Point's history. Its first was Zone Labs, acquired in December 2003 for more than \$200 million.

The Swedish company's solutions are designed to protect laptops, handheld computers and smart phones.

Check Point says the acquisition will help it achieve the next stage in its strategy: adding a new dimension of defense for enterprise data, by protecting portable computing products.

During the first nine months of 2006, Protect Data generated 92% revenue growth to \$52.4 million. Its profit soared 170% to \$8.3 million.

The deal values Stockholm-based Protect Data at SEK 180 per share, or SEK 4.2 billion. Protect Data's shares closed at SEK 175.50 on Friday.

The hefty half-billion and more price tag for Protect Data is no problem for Check Point, which ended the third quarter of 2006 with \$1.61 billion in cash.

Nasdaq introduces Israeli equities index

The index includes over 70 Israeli companies, which have a combined market capitalization of \$50 billion. The Nasdaq stock market has introduced the Nasdaq Israel Index (Nasdaq:ISRQ), which is designed to track the performance of US-listed companies that are incorporated in Israel. Nasdaq began disseminating the index on November 17.

The index includes over 70 Israeli companies, most of which are listed on Nasdaq, and which have a combined market capitalization of \$50 billion.

"This index will serve as a powerful metric by which investors can track the performance of Israeli companies that have attained extraordinary achievements in areas as wide-ranging as manufacturing, agriculture, and high technology," said Nasdaq Executive Vice President John Jacobs. "The companies in this index have played a critical part in Israel's increasingly influential role in key sectors of the global economy."

Charlotte Crosswell, Head of Nasdaq International said, "The index highlights Nasdaq's 25 years of activity and commitment to the Israeli market. We are confident that the index will further enhance the visibility of the Israeli companies among US and international investors as well as help investors from around the world look to invest in the Israeli economy."

The index is calculated using a modified market capitalization methodology. The index will be calculated and disseminated on a price return basis (Nasdaq:ISRQ) and a total return basis (Nasdaq:ISRX).

Computer and software giant Hewlett Packard

Co. (HPQ.N: Quote) said that its largest research and development center will be located in Israel in the wake of its acquisition of Mercury Interactive.



HP bought Mercury for about \$4.5 billion in stock in a deal that was completed earlier in November.

Thomas Hogan, senior vice president of HP Software's technology solutions group, said HP has opted to keep

Mercury's 700 employees that had worked in its offices in Yehud, a town near Tel Aviv, which will bring HP's workforce in Israel to more than 3,000 -- the second largest tech firm after Intel (INTC.O: Quote).

"HP is committed to Israel," Hogan told a news conference a few miles from Tel Aviv. "We have made a decision to continue and maintain operations in Yehud ... The people based in Israel will be responsible for HP's technology moving forward.

"The R&D center in Yehud will be our largest in the world," he said. "This operation is the best of the best."

Boaz Chalamish, the global head of R&D for HP Software, said the Yehud center will now have a much broader portfolio of products to produce.

"It will do everything it did but with much faster execution," he said.

The deal to buy Mercury was HP's largest since a \$19 billion buyout of Compaq in 2002. It also matched the largest foreign purchase involving an Israeli company.

The merger moved HP to the sixth largest software company in the world in terms of revenues.

Applied Materials Israel in \$110m China deal

Semiconductor equipment giant Applied Materials Inc. (Nasdaq: AMAT), through its independent production quality control business division, Applied Materials Israel, will sign an agreement tomorrow with Chinese company SMIC worth \$110 million.

The deal, notes Applied Materials Israel, is the largest which the company has closed since it began operation here 10 years ago.

Applied Israel operates in the field of Process Diagnostics and Control (PDC) and develops and produces testing and control systems which identify flaws in silicon wafers. Applied Israel's products are relevant to semiconductor giants that manufacture huge quantities of chips at an investment of billions for production lines.

SMIC is the third largest provider of outsourcing for integrated circuits to third parties in the world. Under the current agreement, SMIC will buy Applied's UVision system which became available several

months ago, to provide quality control for printing 65 nanometers integrated circuits. SMIC will also acquire the SEMVision system for automatic flaw diagnostics

FIRST U.S. HEDGE FUND, MANAGING \$4 BILLION IN ASSETS, MAKES ENTRANCE INTO ISRAELI MARKET (10/2006)

Old Lane buys stakes in Hydro-Industries

The acquisition represents one of the first entrances of a large hedge fund into the Israeli market and is the first time that a U.S. hedge fund has made an investment in an Israeli technology company. Old lane acquired 9% of the stake in Hydro-Industries. Hydro-Industries has developed proprietary technology that utilizes water pressure to generate kinetic and other forms of energy.

ISRAELI RESEARCH ON HUMAN EMBRYONIC STEM CELL IS RANKED 2ND IN WORLD (10/2006)

According to journal Stem Cells, Israel has the 2nd highest number, in absolute terms, of publications on stem cells in scientific journals

Israel was ranked by the journal ahead of the UK, Korea, China, Singapore, Australia, Sweden and Canada for number of publications on stem cells in scientific journals. Stem Cells also ranked the best human Embryonic Stem Cell (hESC) research papers ever published in peer-reviewed journals, four of which were written by Israelis.

World Bank ranked Israel 5th best for investor protection

Israel is ranked as the easiest country to do business with in the Middle East and North Africa

The World Bank report maintained Israel's overall ranking of 26 for its business environment, out of 175 countries. Israel ranked 7th for the ease of receiving credit, 13th for ease of trading across borders and 15th for ease of starting a business.

Swiss pharma giant expands activities in Israel

Serono seeking additional R&D investment in Israel

The company is currently constructing a new facility in Yavne, Israel which is expected to increase the recruitment of researchers. Giampiero De Luca, Chief Intellectual Property Counsel at Serono said that the company's past investments in Israel created hundreds of millions of dollars in direct revenue and royalties mainly due to the sales of the Multiple Sclerosis drug, Rebif (Interferon). This announcement

came at a conference on Swiss-Israeli collaboration in the Life Sciences industry held in Zurich on September 6th. The conference was organized by the Swiss Organisation for Facilitating Investments (SOFI) and Israel's Ministry of Industry, Trade and Labor. Seventy five Swiss companies, funds and Investment institutions participated in the conference. The Israeli Life Sciences industry has seen strong growth this past year with pharmaceutical exports surging 60% to \$1.4 billion in the first half of 2006.

Unconventional, but Orthodox

In a recent article in thew San Francisco Chronicle we read an article of interest and we are passing it on to you.

When a major property company decided to purchase a prestigious Manhattan skyscraper a couple of years ago, its managers faced the challenge of reading through the 200-page contracts of each of the building's 300 tenants before they could finalize the deal.

It was the kind of back-office paralegal work that could have taken weeks and cost a small fortune. But thanks to the initiative of a New Jersey businessman, the work was carried out in a couple of days a third of the way around the world by a dedicated team of ultra-Orthodox Jewish women, at a fraction of the cost.

This work, known as lease abstracting, is one of the mainstays of Citybook Services Ltd, a company in the ultra-Orthodox -- or "haredi" -- township of Modiin Illit on the edge of the Israeli-occupied West Bank, halfway between Jerusalem and Tel Aviv.

Citybook is a flagship company in Israel's fast-growing outsourcing sector, which takes advantage of the country's large immigrant community to provide English, French, Spanish and Dutch language back-office services to companies in the United States and Europe, including paralegal and accounting work, call centers, graphic design and software development.

Salaries are 40 to 50 percent lower in Israel than in the United States, and because of the time difference -- 10 hours later in Israel than in California -- work can be commissioned at the end of the working day in America, completed overnight during Israel's daytime hours and be ready for stateside clients by morning.

IDT, a Jerusalem company, leads the outsourcing sector, with 1,000 employees operating call centers for clients around the world in a wide variety of languages.

In a 2004 survey, consulting firm AT Kearney ranked Israel as one of the top 25 most-attractive places worldwide for outsourcing. In February 2005, the Economist ranked Israel in the top 20 and in September 2005, Red Herring magazine called Jerusalem a "new hotspot" for outsourcing.

Citybook's arrival in Modiin Illit has not only benefited its clients, it has also set off a small social revolution, providing 150 jobs for women in the impoverished ultra-Orthodox sector, in which more than half of families are below the poverty line -- about \$1,000 per month for a family of four -- and many of the men are full-time students in yeshiva seminaries.



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