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How did the revolution pass us by?

That's the question panelists at this week's IVA conference tried to answer. X-Technologies CEO Guy Shinar went so far as to recommend Israeli funds set up companies anywhere but in Israel.

Aviva Mishmari 10 Apr 03 17:14

It was a pleasant week for the Israeli venture capital industry at the Israel Venture Association conference, shmoozing in the lecture halls, munching to the sounds of bluegrass music, and announcing joint ventures. The creation of BioLine Therapeutics was announced on the first day of the conference, and the Technion Entrepreneurial Incubator Company (TEIC) announced it had been privatized the following day.

With all that, the biotechnology panel was still only half full (or only half empty, depending on how you look at it), but a few pearls of wisdom were nonetheless uttered. Those sitting around the table - managers, investors, and consultants - tried to explain why, as they put it, "the revolution had passed Israel by." A graph comparing investments in US and European life sciences companies with those in Israel was screened. It looked like the elephant versus the mouse.

Israel Seed Partners general partner Neil Cohen then confessed to the funds's guilt: "Why haven't [Bio-Technology General](#) (Nasdaq: [BTGC](#)), Peptor, and XTL Biopharmaceuticals (LSE: XTL) made it yet? Because instead of giving a company enough money to work for a while without constant worry, we find ourselves trying to squeeze every penny. Unless we give them enough to go the distance, we won't achieve the success of which we're capable."

Cohen says that most of the major life sciences funds have \$400-900 million, and the money goes mostly to today's trend: spin-offs from pharmaceutical companies or investments in products only. "This affects us," Cohen said, referring to all his colleagues. "We can't take Israeli companies there. If the company has no Stage 2 drugs, it's of no interest to them. It takes \$10-20 million to reach Stage 2. Unfortunately, today's Israeli funds usually don't have enough capital for this stage. Cohen declared he had no good solution for this problem, and since he had promised not to talk about the need for government aid, he left it at that.

Sad molecules, happy catheters

The start-up people on the panel had no good solution, either, except for the realization that regardless of any success they have in raising money from Israeli funds, they still must seek their fortune overseas. Cooperation with global giants could be a substitute for Israeli companies' reliance on venture capital, says ZetiQ Technologies president and CEO Dr. Dan Gelvan. He says his company has signed cooperation deals for eight or nine pilots, of which "some have commercial value."

How much this will contribute to company revenue is uncertain, but the focus appears to be long-term. Gelvan says ZetiQ is currently burning less than \$6 million a year, but spends 15-20% of its annual budget on business development, even at the cost of R&D. Business development means ceaseless travel to the US and scurrying to conferences and exhibitions, just to get exposure, while picking up some good advice from professionals happening to see the company presentation. "Considering the number of unpaid advisors I got that way, it was worth it," Gelvan comments.

TransPharma Medical CEO Dr. Dapha Heffetz says good things are happening at her company. She repeated Gelvan's advice to reach cooperative agreements as early as possible, in order to obtain recognition from the funds. This may constitute a premature breakthrough. In any case, the price of the product should be determined already at these early stages. A list of global companies that may need the company's technology should be drawn up, a prototype built, and other details, usually left for later, settled. All this is designed to gain a foothold with the major firms. According to Heffetz's description, such a foothold also requires preliminary meetings with the US Food and Drug Administration (FDA), aimed at achieving basic recognition. This means traveling overseas "at least twice a month", and finding the right person in every major company visited.

Gelvan broke in at this point to say, "Until you find someone in the fund, one person who says, 'I'm responsible for this deal', or one person in the company who thinks that investing in you will help him in his project, nothing will happen. You need a personal dimension in the relationship - "people who will take you under their wing." If it turns out that your champions aren't powerful enough to put through a deal in their organizations, the deal will stall.

Once the deal, investment, or cooperative venture has been signed, it will be like the partner wants it to be, i.e. not the way the start-up wants it to be. When they hear this, the venture capital people in the hall shake their heads no. Shortly afterwards, Gelvan says, "A start-up must show flexibility in closing a deal," to which heads were nodded yes. It's all in how you put it.

The panel agreed that Israel's relative advantage in medical technology (med-tech) could be one source of salvation. The ratio of biotechnology investments to med tech investments is 4:1 in the US and Europe, but 1:4 in Israel. That means for every molecule in Israeli going without money, there is an imaging device or sophisticated catheter with a chance to break through. The med-tech people then conducted their own panel.

Challenge Fund - Etgar managing partner Gil Hermon relies on figures showing that early stage financing rounds by Israeli companies averaged \$2.2 million last year. Hermon says he'd like to see that figure rise, giving the company enough money to operate without headaches for at least two years. Like the other investors, he, too, is torn between giving the start-ups a lot of rope, and working very closely with them.

In addition to the money itself, the company valuations for financing rounds and acquisitions are a problem in themselves. Here, too, the average amount is quite embarrassing, compared with US start-ups. Virtually everyone agreed that Israeli technological development is on a par with its overseas equivalents, but the cash available to recompense them is inadequate. Remon Medical Technologies CEO Hezi Himelfarb, however, says, "Nothing can be done about the valuations." It's a matter of the market, he declares; every valuation is a function of the market conditions, and is determined by current climate. Today, the external value of a young life sciences company is usually less than \$10 million, or \$20 million at the most, and that's probably how it will stay. Even so, raising money takes 12 to 18 months these days, and practically requires a miracle.

X-Technologies president and CEO Guy Shinar surprised everyone by proposing that entrepreneurs and funds set up their companies in the US from the beginning. Shinar himself gave up his overseas residence after selling his company, and continues to manage X-Technologies from Israel. With the exception of Shinar and two other employees, the entire company is in the US. Shinar says the best thing for venture capitalists to do is invest in a two-person company and set it up "in the US, around the world, it doesn't matter where," as long as it's not in Israel, where managers must cope with jetlag, management culture gaps, language problems, and the need to direct people and products by remote control.

If only he were wrong.

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