



# Angels over Tel Aviv

The White City has become one of the world's most vibrant start-up ecosystems with angel investments playing an important role



**"ANGELS OVER** Berlin" was German director Wim Wenders' 1987 film about invisible immortal angels who comfort distressed Berliners. Today, in 2016, there are real angels over Tel Aviv.

They are investors and they definitely help distressed start-up entrepreneurs seeking

scarce initial capital and needing wise advice. They are complementing, and to some extent replacing, venture capital, and are growing in importance, both in Israel and abroad. Here is a brief guide to this interesting growth industry.

*What is an angel investor?*

An angel investor is someone who has wealth and is willing, as an individual, to invest it in a high-risk business start-up in return for shares. The latest trend is for angels to band together, to "network" as venture capitalists do, to exchange information and reduce risk, because three heads or 10 are



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better than one.

The name “angel” comes from Broadway, where it describes those who fund musicals and plays, usually strapped for cash and seeking last-resort divine help. Often, angels are entrepreneurs who made a fortune in an “exit” and recycle their profits in funding

other start-ups. They often live and work close to the start-ups in which they invest.

In Israel, there are an estimated 500 angels and their number is growing. Of those 500, perhaps a third are among the “elite,” sought-after and professional. It is hard to find hard data on the total money they in-

vest, but it is probably close to that of venture capital. But, unlike venture capital, angels invest smaller sums in far more start-ups. In the past five years, according to the Israel Venture Center database, angels have invested in 1,600 start-ups. Most of those probably would not have survived a day



without the angels.

An interesting angel innovation is iAngels, started by entrepreneurs Mor Assia and Shelly Hod-Moyal in early 2014. They guide small angel investments in start-ups, by experienced investors who share information and insights. Russian billionaire Roman Abramovich, the Jewish owner of the English premier league soccer team Chelsea, has invested \$2.25 million in iAngels.

The US Center for Venture Research estimates that US angel investors pumped \$24 billion into 73,000 small businesses in 2014, mostly in start-ups. Some 300,000 people have made an angel investment in the US. With four million Americans having net worth of \$1 million or more, qualifying for angel status, those numbers will doubtless grow.

Angel investment is booming in China, too. The number of wealthy Chinese (those with investable assets of \$1.6 million or more) has more than doubled since 2010. The recent Chinese stock market plunge, along with Prime Minister Li Keqiang's call for "mass entrepreneurship," has created a start-up stampede and a boom in angel investments. Some 4,000 businesses are launched daily in China, or 1.6 million in 2014. With Chinese venture capital relatively underdeveloped, angel investments are filling the gap.

*Do angels make money?*

Despite the high risks, some do. A research report shows American angels lost some or all their money in half their deals, when start-ups failed. But another study showed that on average, angel investments returned more than double their investment within four years, and had a rate of return of about 22 percent. No wonder growing sums of money are attracted to angel investing in this era of near-zero interest rates.

Leading angel investor Gigi Levy-Weiss told the Tel Aviv business daily *TheMarker* that not all hi-tech investments pay off. "The top 10 venture capital [VC] firms in the world make high returns," he said, "but the median VC firm is not profitable. The same calculation applies to angels."

*How do angel investors differ from venture capitalists?*

In several ways. First, and perhaps foremost, they are more patient. A venture capital fund generally must close and return profits to its investors in five to seven years. This makes VCs impatient. Often, start-ups are pressed by VC investors to agree to an "exit" (acquisition), so that VCs can also exit

with their money and pay off investors.

This has contributed to the fact that Israel has been unable to grow a single major sustained global company, from start-up size, for more than two decades. In contrast, angel investors have no five-to-seven year deadline, and can thus build their start-up into an independent company over a decade or more.

## THE COMMON THING BETWEEN BUSINESS PLANS AND SAUSAGE IS THAT ONLY PEOPLE WHO DON'T KNOW HOW THEY ARE MADE ARE WILLING TO DIGEST THEM

Second, time and savvy. I once led a group of Israeli managers on a benchmarking trip to Silicon Valley. We went to one of the leading VC firms there and heard a brilliant presentation by a senior partner.

I asked him, how many start-ups he was personally invested in? Thirty, he replied. I made a quick calculation. Start-ups need to have board of directors meetings once a month because they must move rapidly. So this VC partner had to attend 30 board meetings a month, or one a day? Impossible. How much time could he allot to each of his start-ups? Perhaps a few hours a week, if that. It is not enough.

Angel investors, in contrast, can focus on their start-up and give it individual hands-on attention, holding the hand of the entrepreneur. Often this is more important than the actual dollar investment itself.

A Harvard Business School study by Prof. Josh Lerner and colleagues shows that start-up firms funded by angels are less likely to fail than companies that rely on other forms of initial financing, such as venture capital. "The bundle of inputs that angel investors provide have a large and significant impact on the success and survival of start-up ventures," note the authors.

Angel investments provide as much money as venture capital in the US, but since they invest smaller initial sums they fund more

than 60 times as many companies as VCs. This is true in Israel, as well.

*Who are Israel's top angels?*

Two names come to mind: Gidi Levy-Weiss and Yossi Vardi.

There is wide agreement that Vardi is the pioneer, or father, of angel investors in Israel. Vardi, 73, has founded and invested in more than 86 hi-tech companies over the past 20 years. He founded his first start-up 45 years ago and has been an angel investor since 1996. Vardi is also one of the funniest and most insightful speakers, sought after all over the world.

Vardi, a Technion graduate, launched Advanced Technology Ltd. in 1969, one of Israel's first software houses and has served in several high posts in government and industry. He invested in Mirabilis (in Latin, "wonderful") in 1996, started by his son Arik and three partners, offering the first instant messaging application. And wonderful it was!

Just 19 months later, Mirabilis, having never earned a single dollar in revenue, was sold for more than \$400 million to AOL, an American mass-media company. *Forbes* magazine observes that a whole generation of young Israelis sought to create similar miracles. Vardi quips that this miraculous investment "made me blond and good-looking like Ryan Gosling." Since then, he recounts, he has had another 25 exits.

**I ASKED** Vardi for his advice, his secret-sauce recipe, for successful angel investment. His answers were rather surprising.

*Yossi Vardi, what is the key to being a great angel with gilded wings?*

Some of my investments have been idiotic, some embarrassing... Some both idiotic and embarrassing. I do very early seed investments. So far I have invested in around 80 different companies. Some of them fared very nicely and had very glorious exits. My companies were sold to Microsoft, Yahoo, AOL, eBay, Cisco, Sierra Wireless and some of them went public.

Some of them also failed equally gloriously. I have a very impressive list of failures... I have passed on chances to invest in companies that were valued at \$5 million that then sold for \$1 billion! So there's a whole mix of experience. But if you can't stomach the risk, this isn't the game for you...

"Angel investors have to come to grips with the very unflattering reality that the common thing between business plans and sausage is that only people who don't know how

they are made are willing to digest them, that there are more fools among the buyers than among the sellers, that ideas are over-rated, that you are dealing with something which resides in the brains of two or three people and, very often, it is not clear even to them. In short, it is more a gambling than a profession.

“The way to go about it is to approach the whole thing very unemotionally, very technically. If you fall in love with an idea or with an entrepreneur, remember the old French saying that love is blind.

“My approach focuses on a high volatility, diversified portfolio – invest equal sums in all your investees and hope for luck. If you are lucky, you will lose your money on most investments, but if you make many times your investment on a few, it will cover for it.

“In order to sweeten the bitter taste of failure a bit, invest in people who are nice – at least when you lose money you will have the feeling that you helped someone who deserved it. Focus on talent, talent, talent, talent! And last, but not least, the first money invested is the most expensive money, since its [equity stake] is diluted very fast [by future investments]. Therefore, go with entrepreneurs who are careful in spending money in the early phases.”

Vardi has become famous for his “shtick” on Jewish mothers – Jewish mothers are responsible for the Israeli tech scene. Here is how he put it to a reporter from Venture Village, a website.

“What makes Israel the success it is in the tech scene today? Is it the army? Is it the tech academies? All of these are contributing, but I think it is the spirit and upbringing of the young people.

“If your mother is telling you all the time that you have to thrive and you have to be independent and you have to go and study, then this is the value system. The Jewish mothers in Israel have a very effective way to manipulate their offspring – my mother used to tell me all the time that I’m an idiot and that all my cousins are really smart, and I’ve spent all my life trying to prove her wrong. I am still trying to prove it to her, even though she died 15 years ago.”

Vardi told me that VCs and angels are “totally different things. Angel investors are willing to take much higher risks, enter much earlier, buy stock [in start-ups] on terms much more favorable to the entrepreneurs than VCs, and VCs are usually willing to invest only when there is

some proof of viability.”

But he also poured some cold water on the “hand-holding” aspect of angels. “Regarding [management] help – I don’t promise any help. I promise a certain amount of funding and stand by it. If I have a chance to help, I gladly do it, but I am very keen not to raise expectations. I like to under-promise and over-deliver.”

## IT WOULD BE WELL TO REMEMBER THAT TEL AVIV COMPETES WITH MANY OTHER CITIES WORLDWIDE TO ATTRACT BRAINS AND TO FUND AND SUSTAIN THEIR IDEAS

The number of Internet start-ups is growing. Angel funds are partly a cause, and, in part, an effect. Vardi notes, “Angel investing is very suitable for early stage Internet investments, where in the last 10 years, funding requirements have shrunk to an amazingly low level, and there are some good reasons why it happened. This is not the case in other industries where initial larger amount of funds are needed, like infrastructure investments.”

I was privileged to work, through the Technion Institute of Management, with Levy-Weiss, a former IDF pilot and, in my opinion, super-genius, when he headed 888, an Israeli online gaming company. Before that, he was a senior executive with software giant Amdocs.

TheMarker lists Levy-Weiss as Israel’s No. 1 Angel. He is networked with 44 other angels and has made new investments in 67 start-ups, between 2005 and 2015. Like many angels, he invests primarily in Internet start-ups.

Recently, Levy-Weiss set up an accelerator in Silicon Valley. Israel itself has more than 80 such accelerators – places where start-ups get mentoring, advice, office space, some funding and learn to pitch their ideas to investors.

Writing about angels in TheMarker, Inbal Orpaz draws attention to the gender

issue. “Only 7.5 percent of start-up entrepreneurs in Israel are women,” she notes, “and only three out of the 180 top angel investors are women.” In contrast, in 2015, nearly one angel in five in the US was female, up from one in eight in 2012.

Tel Aviv has become one of the world’s most vibrant start-up ecosystems, ranking fifth in the world, behind Silicon Valley, New York, Los Angeles and Boston, with angel investments playing an important role. I asked Vardi about how to create such a tech hub.

“How do you become a tech hub? You obviously need technology, money, education etc., but many places that have these attributes don’t become a tech hub. You need the culture of the young person – what do they dream of at night? Working in hi-tech is no longer a job – it’s part of their lifestyle. Start-ups are moving to city centers, taking laptops to the coffee shops.

These people are looking for cities that are underground, cultural, chaotic. They want cities to accommodate different people, genders, tastes, as they bring different DNA into the game and that’s very important – they want the cities to be very permissive,” Vardi says. He cites Berlin as an example.

Wim Wenders’ angels still hover over Berlin. Many young Israelis are drawn to Berlin’s magnetic energy, and Berlin attracts fully two-thirds of all risk capital invested in Germany. While there are many angels in Tel Aviv, angels hover very visibly abroad over other cities, as well, seeking creative brains and novel, useful ideas, and drawing talent from everywhere.

It would be well to remember that Tel Aviv competes with many other cities worldwide to attract those brains and to fund and sustain their ideas. We should do everything possible to keep those brains, and the ideas, jobs and wealth that flow from them, at home.

*Postscript:* On December 29, the Knesset Finance Committee approved an amendment to the 2010 Angels Law, assuring angel investors they will receive immediate tax benefits. The Law itself provides tax relief only three years after the initial investment. Hence, it was ineffective. ■

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