From START-UP NATION to MULTINATIONAL PLAYER

BY ADI RIMON, SIOR

ISRAEL'S LOCAL MARKET STRENGTH EXPANDS ITS GLOBAL CRE FOOTPRINT

Israel's economy is a highly advanced, primarily knowledge-based economy. The country's major economic sectors are high tech and specialized industrial manufacturing. Historically—with no natural resources or geographical trade routes of significance—Israel has come to rely on human resource and ingenuity to drive its economy forward in the global arena.

With the second-largest number of startup companies in the world after the United States, Israel's high tech sector is regarded competitively on par with that of the Silicon Valley. The success of the sector over the past two decades has earned it the title of "Start-up Nation." Global giants such as Intel, Microsoft, and Apple built their first overseas research and development facilities in Israel, with other high tech multinationals such as Facebook and IBM following suit in recent years. This was helped by the fact that Israel's economy

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was ranked as the world's most durable economy in the face of geo-political and national security crises.

As with the rest of the world, the novel Coronavirus pandemic has hit Israel's high tech industry—and thereby the local real estate market—though not everyone has been hit equally. Israeli high tech entered the Coronavirus crisis armed with a lot of capital. As opposed to the global financial crisis of 2008, a lot of venture capital (VC) funds have money to spend. Most of that money was slated for new startups, but VC funds traditionally give priority to existing portfolio companies—a priority that has taken on new urgency amid the Coronavirus lockdown. The money does not have to come from inside Israel; the rest comes from overseas, mainly the United States. Whether from Israel or from abroad, the funds will continue to invest in high-tech, even in these troubled times.

It is still too early to tell what the full impact of COVID-19 will be on the economy, but from a CRE prospective, this continued investment activity suggest that the real estate market will rebound in a comparatively short time. It might not come back to what it was before the pandemic, and the volume and nature of real estate demand from occupiers, landlords, investors, and developers may change, but what's certain is that the outlook for Israeli CRE now is less apocalyptic than it was at the onset of the crisis.

This multinational inbound activity has facilitated strong demand for quality office, and research and development (R&D) space in Israel's local CRE market, with increased average rental prices and occupancy rates. Local building development in 2019 saw a record number of new project starts. Additionally, it has surged outbound activity. As a leading tech powerhouse, more and more Israeli entrepreneurs opt to build their businesses abroad, to tap into international markets and locate near strategic clients. There is also a growing layer of maturing Israeli companies that scale-up globally and stay independent. Rather than acquisition by larger multinationals, these companies set-up shop in major global high tech hubs, leasing considerable amounts of space for their activities and acquiring local companies to expand in those markets.

Israel boasts the third-largest number of NASDAQ-listed companies after the U.S. and China. A significant number of these firms are Biotech, Pharma, and specialized industrial companies that manufacture and distribute their products worldwide. According to the Organisation for Economic Co-operation and Development (OECD), Israel spends more money on R&D as a percentage of its GDP than any other country, other than South Korea. While R&D is mostly carried out in Israel, a relatively small local market for their products, high wages, and geographical supply-chain limitations mean that Israeli multinationals need to expand their manufacturing and logistical CRE footprint abroad in order to grow. It is estimated that over 80% of Israeli industrial multinationals have production and/or warehouse sites outside of Israel.

This outward-looking expansion is helped by well-established global business ties between Israel and the leading economies of the world. According to the U.S. Bureau of Economic Analysis, Israel was the 13th largest source worldwide for foreign direct investment (FDI) into the U.S. in 2016 at $55.4 billion. For Israeli companies, direct access to local U.S. clients—saving money on transporting and shipping goods, and the ability to ship products to customers quickly—is an important part of why they build their facilities in the U.S.

Another reason is the incentives offered by local and state governments to establish sites in specific locations. The European Union is Israel's biggest trading partner with most local market standards mirroring those in Europe. Thirty percent of Israel's exports and 50% of its imports relate to the European market. Given the growing intensity of economic activity and the geographic and cultural proximity between Israel and Europe, it is no wonder that many Israeli companies operate production, warehouse, and office facilities in Europe to access the local markets. China is Israel's largest trade partner in Asia and its third largest global trading partner after the EU and the U.S., with mutual trade estimated at $11 billion as of 2016, according to the Israeli Foreign Ministry. China-Israel business activity has been buzzing over the past decade as China's interest in the start-up nation's technological know-how has grown, and as Israeli entrepreneurs increasingly eye the huge potential in China's growing consumer market. Additionally, many Israeli industrial multinationals have opted to set-up production facilities in China for its still relatively low-income labor market.

For CRE professionals—both local and international—Israel's economic transformation in recent years, from "start-up nation" to multinational player, presents opportunities to increase business, largely untapped. Multinationals seeking to enter the Israeli market and those already operating in it, will naturally require real estate services to complement set-up and expansion of their local footprint. As real estate is largely regarded as a "local business"—each market with distinct characteristics and best practices—decision-makers at headquarters will undoubtedly rely on established work relations with local CRE professionals to provide advice for navigating the real estate aspects of their activities at their target destinations. The same process applies to Israeli companies venturing and operating in the global arena. Experience has shown that sometimes, these corporations will not devote sufficient attention to the real estate aspect of their destination market. It is up to trusted real estate professionals to ask the right questions, recognizing and pointing out the challenges and opportunities that will have an effect on any company doing business abroad.

MEET THE AUTHOR

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ISRAEL AT A GLANCE			WORLD RANKING
Area	22,072 sq. km	8,522 sq. mi	150th
Population	9,167,380	2020 estimate	99th
GDP	$US 353.6 billion	2019 estimate	32nd
GDP per Capita	$US 43,199	2019 estimate	20th
Total CRE Built	~14 million sq. m	~152 million sq. ft	2009-2018
Total CRE Planned	~2.3 million sq. m	~25 million sq. ft	2018
Average Yearly Rent - Office	$US 372 per sq. m	$US 34.5 per sq. ft	Tel Aviv - Class A
Average Yearly Rent - Industrial & Logistics	$US 172 per sq. m	$US 16 per sq. ft	Central - New
Market Cap Rate - CRE	6% - 7.5%		Office & Industrial

"ISRAEL AT A GLANCE" SOURCES
https://en.wikipedia.org/wiki/Israel | https://www.cbs.gov.il/ | https://www.natam.co.il/natams-report-first-half-2019/