

February 13, 2020

ISRAEL EQUITY REVIEW & OUTLOOK - DEC 2019

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About BlueStar Indexes®

BlueStar Indexes is a leading provider of research and investment solutions for the Israeli capital markets. BlueStar has been producing monthly market updates on the Israeli market since 2012. In our *Israel Equity Review and Outlook* we provide data and insight on recent performance of Israeli equity benchmarks, stocks and sectors driving performance, key economic data for the Israeli market, as well as technical analysis of our flagship Israeli equity indexes, BIGI® and BIGITech®.

The BlueStar Israel Global Index® (BIGI® or BLS & BLSTR INDEX on Bloomberg) is the broadest and deepest benchmark for Israeli equities trading worldwide in Tel Aviv, New York, London, Singapore and Australia. The VanEck Vectors Israel ETF (ticker ISRA) tracks BIGI® and is listed on the NYSE. In addition, Israel-domiciled investment vehicles tracking BIGI® are offered by Psagot and IBI.

The BlueStar Israel Global Technology Index™ (BIGITech® or BGTH & BGTHTR INDEX on Bloomberg) is the broadest and deepest benchmark tracking the performance of Israeli companies operating in innovative sectors like information technology, defense technology, clean technology and bio-technology. The BlueStar Israel Technology ETF (NYSE ticker: ITEQ®) tracks BIGITech®. In addition, there are two Israel-domiciled investment vehicles tracking BIGITech® managed by KSM/Excellence.

BlueStar also maintains five additional Israel Equity Indexes (BIGI®-TIM, IGEI, IDEI, BIGI®-SD and BIGI®-SV), one Israel Government Bond Index (BIGUSD), more than 20 Regional and Global Thematic/Tech Equity indexes, and the BlueStar-TzurGilboa Israel Equity Hedge Fund Index. More than US\$700 million in index-tracking assets are benchmarked to BlueStar Indexes as of end-December 2019.

JOSHUA KAPLAN, CFA*

Director of Research

(646) 380-2503

jkaplan@bluestarindexes.com

STEVEN SCHOENFELD*

Chief Investment Officer

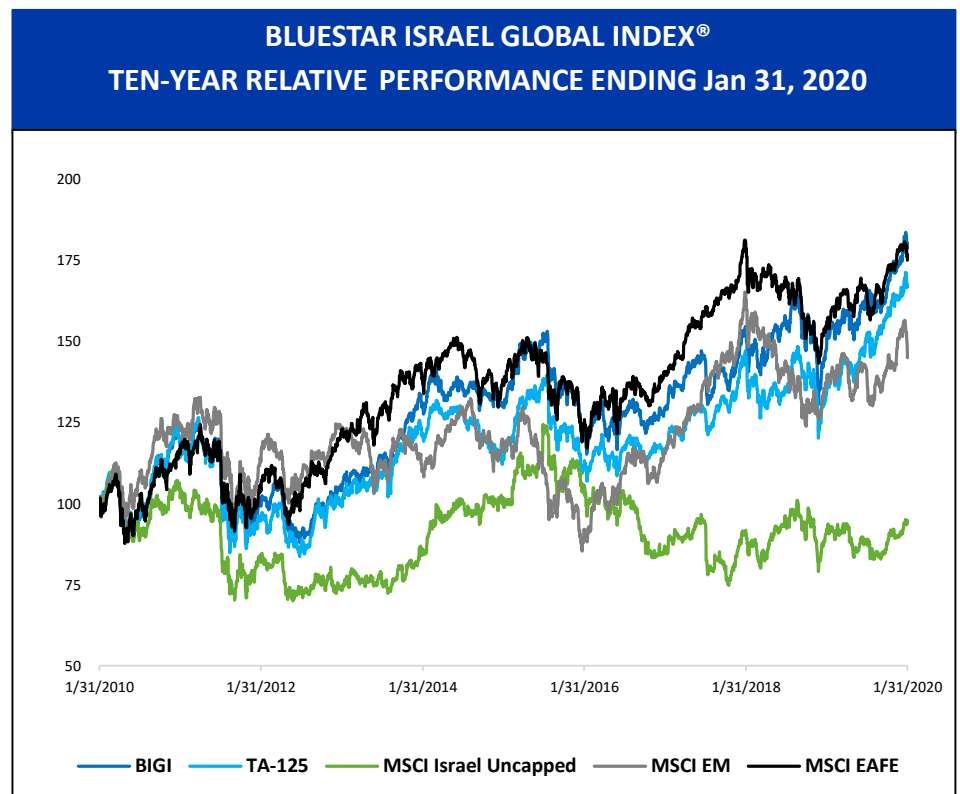
(646) 380-2501

sschoenfeld@bluestarindexes.com

ISRAELI EQUITIES JUMP TO AN EARLY LEAD AGAINST MAJOR EQUITY BENCHMARKS IN 2020. ISRAELI TECH STOCKS CONTINUE THEIR OUTPERFORMANCE FOLLOWING A STELLAR 2019.

Highlights:

- Israeli stocks, as defined by the BlueStar Israel Global Index® (BIGI®), kicked-off the year with a gain of 2.26% in January, outperforming its developed market peers (MSCI EAFE) by 4.35%. BIGI's positive performance in January was in stark contrast to the negative returns of MSCI EAFE (-2.08), MSCI EM (-4.66) and the S&P500 (-0.04), respectively.
- Israeli technology stocks, as defined by The BlueStar Israel Global Technology Index™ (BIGITech®), gained 4.76% in January, outperforming the Dow Jones US Tech and S&P Global Tech indexes, 0.72% and 1.95%, respectively.
- BIGITech's continued growth in January follows an impressive 2019, where it returned 38.95%, making it one of the best-performing global technology indexes.
- BIGI outperformed the flagship local Israeli TA-125 Index by 1.00% in January, as the TA-125 has missed out on the performance of some of Israel's top foreign-listed technology companies.
- 2019's strong performance confirmed the long-term positive technical trend for Israeli equities with January and early-February returns confirming our bullish technical outlook. BIGI remains decisively bullish, with all-time-highs notched in recent weeks. Israeli tech stocks, as measured by BIGITech, consolidated late 2019/early January gains later in January, and have since rebounded.



BONUS: Check out the [brief video highlighting the Israel investment opportunity](#) by our partners at VanEck Vectors.

Israel Equity Market Performance

Israeli Equities, as defined by the BlueStar Israel Global Index® (BIGI®), gained 2.27% in January, leading other international equity benchmarks by a relatively wide margin with relative outperformance in January against MSCI EAFE and MSCI EM of 4.35%, and 6.93%, respectively.

Steep losses in January in Israel's Energy and Materials stocks were outweighed by advances in the Information Technology, Industrials and Utilities sectors. The Information Technology sector contributed 2.19% to BIGI's 2.27% gain as large companies such as NICE, Wix.com, and CyberArk lead the way with gains 11.8%, 16.6%, and 18.5%, respectively.

Israeli technology stocks, as defined by BIGITech® - the BlueStar Israel Global Technology Index™ - were up 4.76% in January putting Israeli tech slightly ahead of the Dow Jones US Tech Index, and well ahead of the S&P Global 1200 Info Tech and MSCI EM Tech indexes.

The major story hitting global markets in January was the outbreak of the deadly Corona Virus. Companies with large exposure to the Chinese market, by way of revenue or supply chain, were hit the hardest. This was reflected in the -10.8% return on Israeli Materials stocks in January. In addition Israeli Energy stocks were down 15% as natural gas prices dropped and potential demand for LNG exports to China was reduced. In early February markets stabilized but the situation remains fluid.

The Bank of Israel in January kept its policy interest rate unchanged at 0.25% as inflation remains muted and initial estimates of Israel's 2020 GDP growth indicate a deceleration. While the labor market remains strong and overall economic indicators continue pointing toward expansion, the political gridlock's impact on government spending is expected to have a slightly adverse impact on overall GDP growth.

These developments point to a period of relatively weak performance for stocks tied closely to Israel's domestic economic growth, while export-oriented sectors like Health Care and Information Technology will need to remain higher to maintain Israeli equities' lead on other international benchmarks for the remainder of 2020.

Another challenge for Israel's economy as a whole, but especially for exporters, is the strength of the Israeli Shekel, which is one of only a handful of currencies that has been appreciating against the US Dollar. Key support for the Shekel is at 3.40/US\$1, and the Bank of Israel has been intervening to hold that level.

Israel's third election in less than a year's time is scheduled for March 2. Despite hopes for a clear winning party, the potential for an inconclusive result remains high. In addition, the lack of a new budget has created a level of certainty in a wide range of areas, including infrastructure, privatization, education and the real estate market. Many observers believe that a broad-based coalition – whether led by the Likud or by Blue & White – would be the most positive outcome for the Israeli economy. BlueStar would like to remind our readers that a solid consensus on a liberal, market-oriented economic policy is shared by *both* major parties, as well as by a majority of the smaller parties.

ISRAEL AND GLOBAL EQUITY BENCHMARK COMPARISON

Benchmark	Jan. Return (%)	2020 (%)
BIGI®	2.27	2.27
BIGITech®	4.76	4.76
MSCI Israel Uncapped	4.74	4.74
TA-125 INDEX	1.27	1.27
S&P 500	(0.04)	(0.04)
MSCI EM	(4.66)	(4.66)
MSCI EAFE	(2.08)	(2.08)
Israel Domestic Exposure	(1.25)	(1.25)
Israel Global Exposure	0.77	0.77
Israel Equity Hedge Fund Index	1.76	1.76

Sources: BlueStar Indexes, Bloomberg LP

ISRAEL AND GLOBAL EQUITY BENCHMARK COMPARISON

Benchmark	Jan. Return (%)	2020 (%)
BIGITech®	4.76	4.76
Dow Jones US Tech	4.04	4.04
S&P Global 1200 Info Tech	2.81	2.81
MSCI EM Tech	(2.36)	(2.36)

TOP AND BOTTOM BIGI PERFORMERS: JAN. 2020

Positive Contributors (%)		Negative Contributors (%)	
Tremor International Ltd	25.63	Intec Pharma Ltd	(41.86)
Altshuler Shaham	25.63	Tamar Petroleum Ltd	(28.14)
Enlight Renewable Energy	22.30	Xlmedia Plc	(21.41)
Kornit Digital Ltd	22.06	888 Holdings Plc	(18.82)
Compugen Ltd	20.81	Energiean Oil & Gas Plc	(17.72)
Gilat Satellite Networks Ltd	18.95	Tufin Software Technologies	(16.88)
Electra Ltd	18.89	Audiocodes Ltd	(16.54)
Cyberark Software	18.57	Israel Corp Limited/The	(16.09)
Energix-renewable Energies	18.50	Clal Insurance Enterpr Hldgs	(15.26)
Shapir Engineerin	16.87	Delek Group Ltd	(14.74)

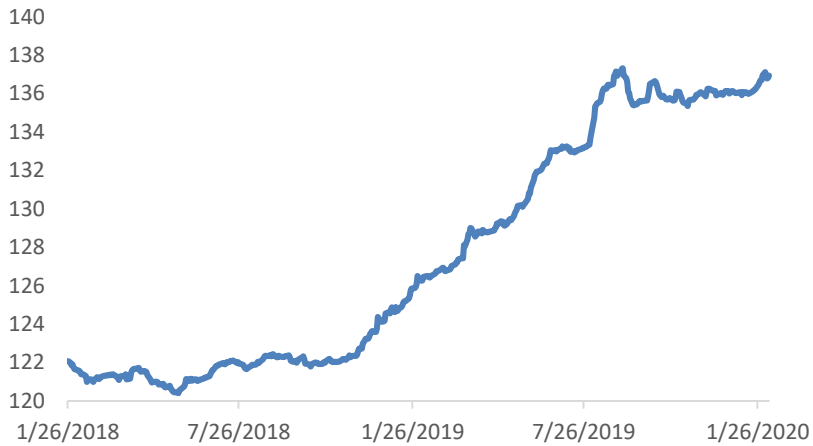
SECTOR PERFORMANCE: JAN. 2020

Utilities	8.54
Industrials	6.16
Information Technology	5.28
Real Estate	2.55
Health Care	0.56
Communication Services	(0.05)
Financials	(0.14)
Consumer Staples	(2.69)
Consumer Discretionary	(5.18)
Materials	(10.88)
Energy	(15.04)

The BlueStar Israel Government USD Bond Index

The attractiveness of Israeli government debt continued in January as the yield to maturity (YTM) on the **BlueStar Israel Government USD Bond Index** (with an average of 5 years to maturity) stands at 1.90%, while the generic US government 5-year bond has a YTM of 1.37%, and the YTM on Shekel-denominated Israeli government debt is even lower at 0.29%. There is growing interest in Israeli government debt due to the planned inclusion of Israel in the FTSE World Government Bond Index series in April 2020.

BlueStar Israel Government USD Bond Index



Sources: BlueStar Indexes, Bloomberg LP

ISRAEL AND GLOBAL SOVEREIGN DEBT COMPARISON (Maturity-Matched)

Benchmark	YTM (%)	Duration
BlueStar Israel Government USD Index	1.90	4.27
US Government Generic 5 Year Bond	1.37	4.29
Israel Government Generic 5 Year Bond	0.29	3.71

Sources: BlueStar Indexes, Bloomberg LP

The *BlueStar-TzurGilboa Israel Equity Hedge Fund Index*: Measuring Long-Short and Long-Only Israeli Stock Funds, the Largest Part of Israel's Hedge Fund Industry

Last summer, BlueStar Indexes partnered with Tzur Management and Gilboa Fund of Funds in launching the first index tracking the performance of Israeli equity-focused hedge funds. The **BlueStar TzurGilboa Israel Equity Hedge Fund Index** is the first and only measure of performance for the dynamic and growing universe of Israeli equity focused hedge funds. It is an equal-weighted index which as of end-August includes 22 hedge funds with combined assets of approximately \$2.5 billion. The index has more than five years of history, starting in January 2014, and is a sub-component of the multi-asset class **TzurGilboa Hedge Fund Index** which includes 65 funds, with more than twelve years of history from January 2007.

The **BlueStar-TzurGilboa Israel Equity Hedge Fund Index** is comprised only of funds that meet the minimum assets criteria, are established as a hedge fund structure, and are focused on investing primarily in Israeli publicly-traded equities. A chart of its performance compared to the BlueStar Israel Global Index® shows its historical outperformance, and a comparison of its volatility to BIGI® shows its potential for diversification.

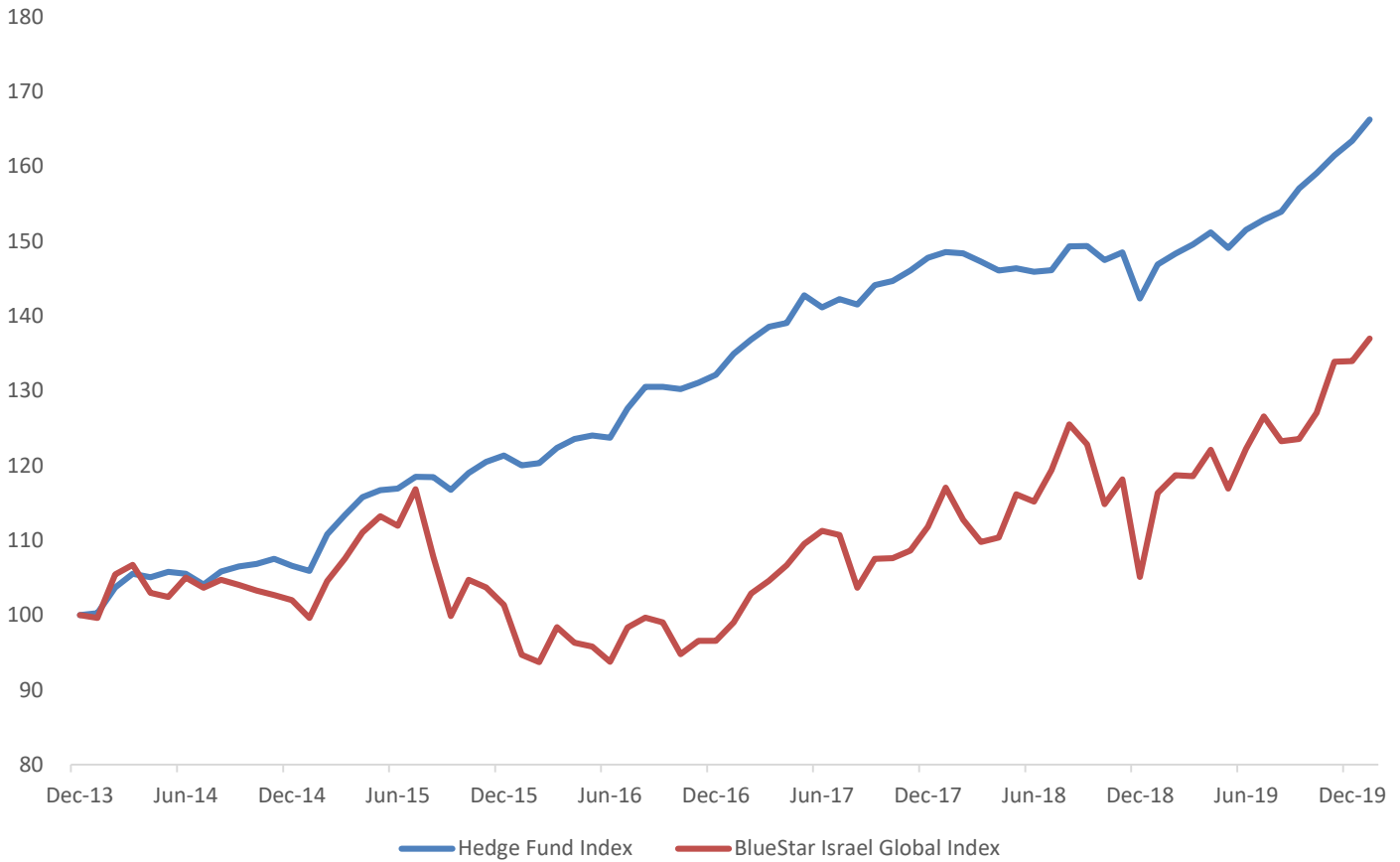
The Israeli hedge fund industry grew rapidly last decade – at a 19% annual growth rate of assets under management (AUM) - with more than 150 hedge funds and \$6 billion of AUM, according BlueStar partner **TzurGilboa's 2019 Survey of Israeli Hedge Funds**. More than 20 managers have assets over \$50 million, and all key hedge fund strategies are represented, including fundamental long/short, quantitative equity, global macro, FX, fixed income/debt, activist and distressed assets. We expect further growth in the 2020s.

More than 60% of Israeli hedge funds focus on equities, both Israeli and global stocks, and this category – with the Israeli component tracked by the **BlueStar-TzurGilboa Israel Equity Hedge Fund Index** – has generated the most interest from global investors. The investor base for Israeli hedge funds is diverse, including high-net-worth individuals, hedge fund allocators and institutional investors from around the world. In addition, the Tel Aviv Stock Exchange and Israeli regulatory authorities have launched several initiatives to encourage greater activity by Israeli hedge funds.

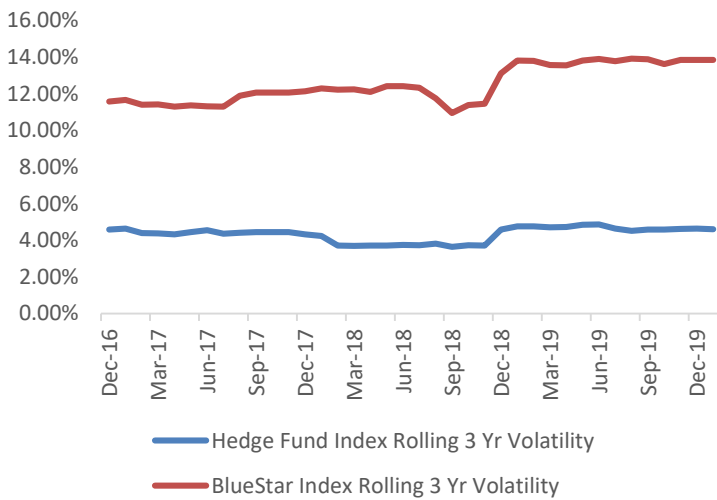
The **BlueStar-TzurGilboa Israel Equity Hedge Fund Index** raises investor awareness of the opportunities to invest in Israeli hedge funds and the Israeli public equity market in general. By encouraging investment in Israel's dynamic asset management industry, this index – along with BlueStar's flagship Israel Equity and Bond indexes - aims to contribute to the development of Israel's capital markets.

The BlueStar–TzurGilboa Israel Equity Hedge Fund Index (data as of January 31, 2019)

Israeli Equity Hedge Funds & Israeli Equities Comparative Returns Since 2013



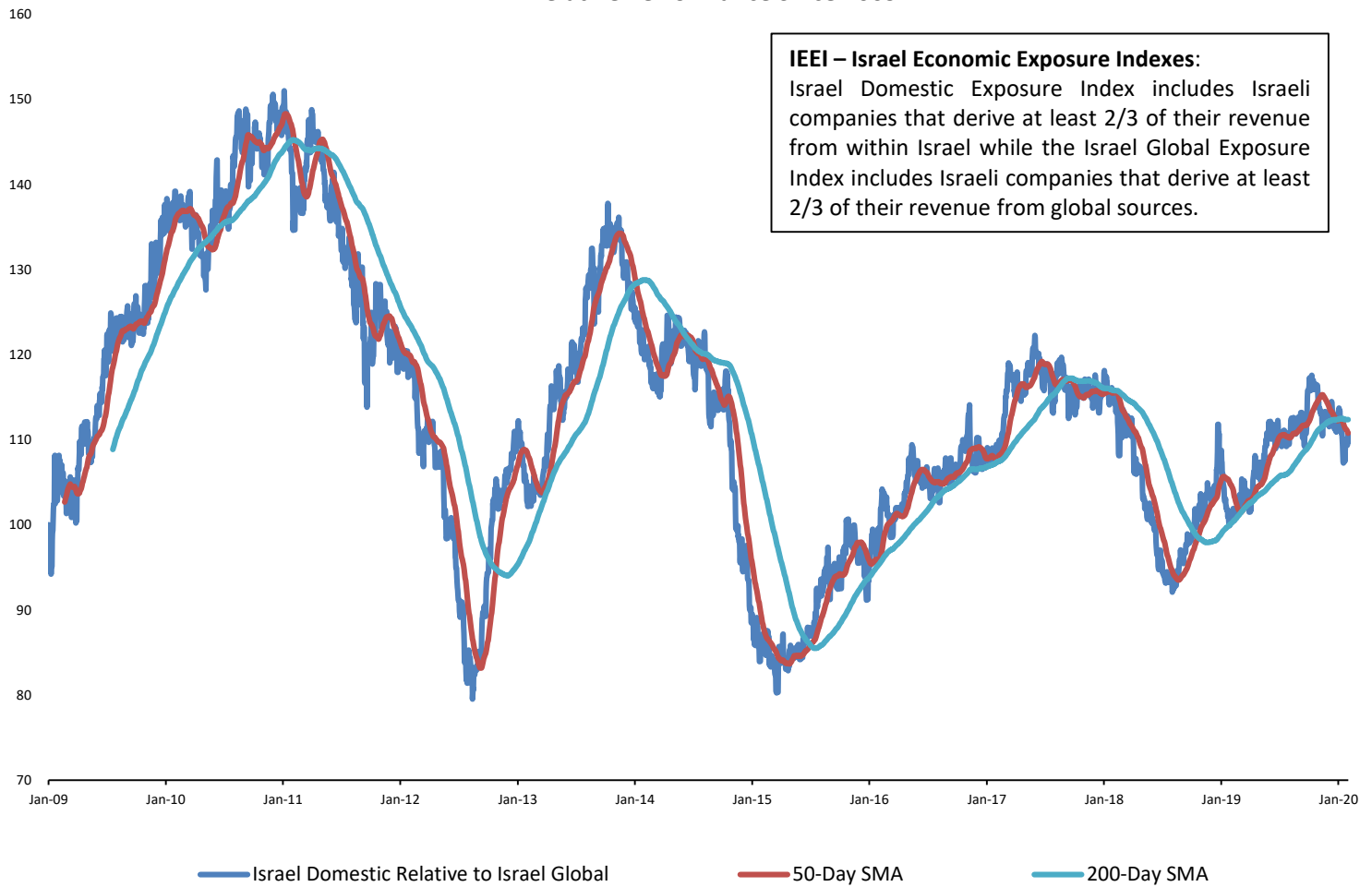
Rolling 3-Year Volatility



Rolling 3 Year Correlation



IEEI Relative Performance Since 2009

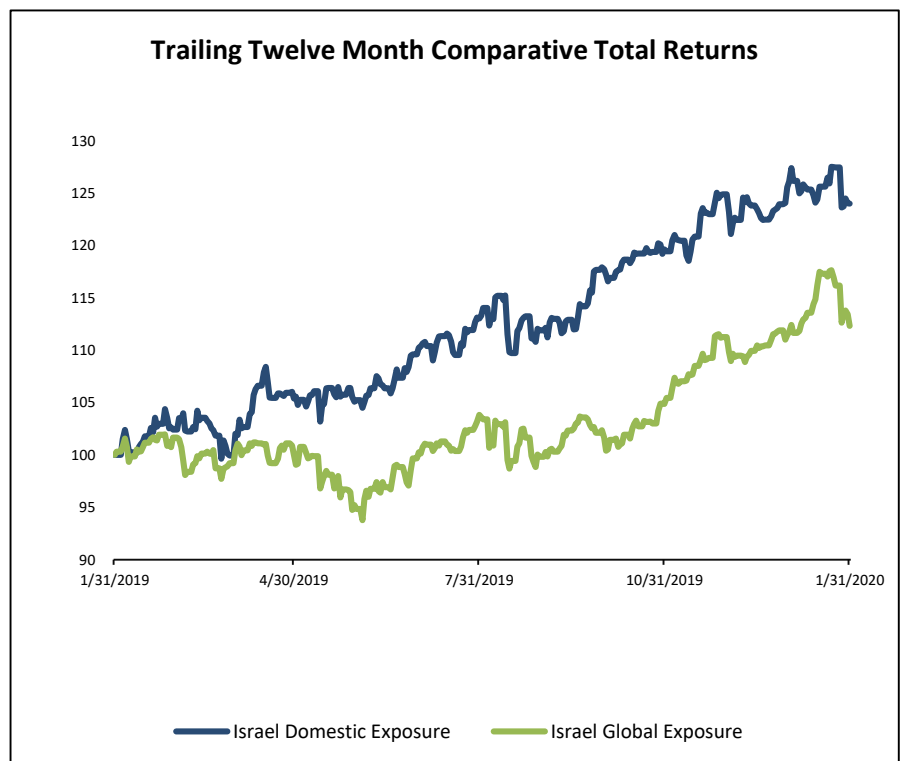


In January, globally-oriented Israeli stocks outperformed their domestically-oriented counterparts by 2.02%. Since our quantitative rotation model signaled that globally-oriented stocks would outperform domestically-oriented stocks in mid-August 2019, the IGEI index has outperformed the IDEI index by roughly 6%.

We believe this trend will continue into the first half of 2020 for two reasons:

First, Israeli GDP growth, while still a leader among Developed Markets, is expected to stabilize in 2020 and 2021. Furthermore Israel's labor market is unlikely to see additional strengthening in 2020 as unemployment is already at a record low but job vacancies are beginning to increase. We feel that on-balance this should put a limit on multiple expansion in Israeli domestically-oriented stocks compared to their globally-oriented peers.

Second, we expect strong momentum in earnings for Israeli tech stocks to carry over from 2019 into 2020, further driving performance of Israeli globally-oriented stocks.



*Sources: BlueStar Indexes, Bloomberg LP

Technical Analysis (Chart data as of February 6, 2020)



BlueStar Israel Global Index®

Israeli Global Equities - as measured by BIGI® - have confirmed their bullish technicals, following healthy consolidation in mid-2019. BIGI's breakout in late October and early November to fresh new highs produced a powerful surge to the upward sloping double-resistance line, were surpassed a second time last month. We continue to expect some consolidation following this run, but the prospects for further highs are strong, with a long-term objective at the lower of the two resistance lines that extend back to 2010. BlueStar's view remains bullish, and we believe that the 370-380 level is an achievable target for later in 2020. Our technical outlook for BIGI® would now only shift toward a bearish view if the double lines of intermediate support at the 2019 breakout level of 315 was decisively broken.



BlueStar Israel Global Technology Index™

Israeli technology stocks - as measured by BlueStar's BIGITech® index - continued their strongly bullish trend and reached all-time-highs in December, and early January. During the coming months they have potential for substantially higher levels, though they are somewhat overbought. It should be noted that 2019 returns of more than 38% made BIGITech® one of the best-performing global technology indexes, and that both Israeli and global investors continue to be attracted to Israeli Tech Stocks.

After a powerful run in the first half of 2019, BIGITech consolidated last Autumn and subsequently surged above its initial 350 target. Following some consolidation back to the red 'speed line,' BIGITech rebounded and is testing all-time-highs as of this writing. Long-term investors who believe in the strong fundamental case for Israeli Technology Stocks should monitor the staying power of this breakout and consider accumulating positions with awareness of the strong confirmed support at the BIGITech 310 level.

*Sources: BlueStar Indexes, Bloomberg LP

Disclosures

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The authors are long, have trading authority over accounts which are long, or may enter into long positions in the following securities which are constituents of BlueStar's Indexes® or track BIGI® or BIGITech®: Amdocs (DOX), CyberArk (CYBR), DSP Group (DSPG), Elbit Systems (ESLT), Teva Pharmaceuticals (TEVA), Israel Chemicals (ICL), BlueStar Israel Technology ETF (ITEQ®), VanEck Vectors Israel ETF (ISRA®) and Defiance Next Gen Connectivity ETF (FIVG).

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