MAGIC SOFTWARE ENTERPRISES LTD
Form 20-F
April 02, 2009

SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

FORM 20-F

o **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934**

OR

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2008

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from __________ to __________

o **SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
Date of event requiring this shell company report

Commission file number: 0-19415

MAGIC SOFTWARE ENTERPRISES LTD.

(Exact name of Registrant as specified in its charter
and translation of Registrant s name into English)

Israel
(Jurisdiction of incorporation or organization)

5 Haplada Street, Or Yehuda 60218, Israel
(Address of principal executive offices)

Amit Birk; +972 (3) 538 9322; abirk@magicsoftware.com
5 Haplada Street, Or Yehuda 60218, Israel
(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Ordinary Shares, NIS 0.1 Par Value	**NASDAQ Global Market**

Securities registered or to be registered pursuant to Section 12(g) of the Act: **None**

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: **None**

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock as of the close of the period covered by the annual report:

Ordinary Shares, par value NIS 0. 1 per share **..31,893,880** (as of December 31, 2008)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes o No x

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer o Non-accelerated filer x

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP x International Financial Reporting Standards as issued by the International Accounting Standards Board o Other o

If Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow:

Item 17 o Item 18 o

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

This annual report on Form 20-F is incorporated by reference into the registrant s Registration Statements on Form S-8, File Nos. 333-13270, 333-11220, 333-1946, 333-10794, 333-113552, 333-132221 and 333-149553.

INTRODUCTION

Magic Software Enterprises Ltd. develops markets, sells and supports an application platform and business and process integration solutions. Our products and services are available through a global network of our regional offices, independent software vendors, or ISVs, system integrators, or SIs, distributors and value added resellers, or VARs, as well as original equipment manufacturers, or OEMs, and consulting partners in approximately 50 countries. Our technology provides our partners and customers the ability to create any type of business application, leverage existing information technology, or IT, resources, enhance business ability, and focus on core business priorities to gain maximum return on their existing and new IT investments. We are known for our code-free approach, allowing users to focus on business logic rather than technological requirements. This approach forms the driving principle of both our uniPaaS application platform and our iBOLT business and process integration suites. Our ordinary shares are listed on the NASDAQ Global Market under the symbol MGIC and are also traded on the Tel Aviv Stock Exchange. As used in this annual report, the terms we, us, our, and Magic mean Magic Software Enterprises Ltd. and its subsidiaries, unless otherwise indicated.

We have obtained trademark registrations for Magic® in the United States, Canada, Israel, the Netherlands (Benelux), Switzerland, Thailand and the United Kingdom. All other trademarks and trade names appearing in this annual report are owned by their respective holders.

Our consolidated financial statements appearing in this annual report are prepared in U.S. dollars and in accordance with generally accepted accounting principles in the United States, or U.S. GAAP. All references in this annual report to dollars or $ are to U.S. dollars and all references in this annual report to NIS are to New Israeli Shekels.

Statements made in this annual report concerning the contents of any contract, agreement or other document are summaries of such contracts, agreements or documents and are not complete descriptions of all of their terms. If we filed any of these documents as an exhibit to this annual report or to any previous filling with the Securities and Exchange Commission, you may read the document itself for a complete recitation of its terms.

This annual report on Form 20-F contains various forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and the Private Securities Litigation Reform Act of 1995, as amended, with respect to our business, financial condition and results of operations. Such forward-looking statements reflect our current view with respect to future events and financial results. Statements which use the terms anticipate, believe, expect, plan, intend, est and similar expressions are intended to identify forward looking statements. We remind readers that forward-looking statements are merely predictions and therefore inherently subject to uncertainties and other factors and involve known and unknown risks that could cause the actual results, performance, levels of activity, or our achievements, or industry results, to be materially different from any future results, performance, levels of activity, or our achievements expressed or implied by such forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. Except as required by applicable law, including the securities laws of the United States, we undertake no obligation to publicly release any update or revision to any forward looking statements to reflect new information, future events or circumstances, or otherwise after the date hereof. We have attempted to identify significant uncertainties and other factors affecting forward-looking statements in the Risk Factors section that appears in Item 3D., Key Information Risk Factors.

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PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

A. SELECTED FINANCIAL DATA

The following table presents selected consolidated financial data as of the dates and for each of the periods indicated. This data includes discontinued operations for certain of the presented periods (see Note 3(a) and 3(c) to the consolidated financial statements). You should read the selected consolidated financial data set forth below together with Item 5. Operating and Financial Review and Prospects as well as our consolidated financial statements and notes thereto appearing elsewhere in this annual report.

We have derived the following consolidated income statement data for the years ended December 31, 2006, 2007 and 2008 and the consolidated balance sheet data as of December 31, 2007 and 2008 from our audited consolidated financial statements and notes included elsewhere in this annual report, with the relevant adjustments due to the discontinued operations. We have derived the consolidated income statement data for the years ended December 31, 2004 and 2005 and the consolidated balance sheet data as of December 31, 2004, 2005 and 2006 from our audited consolidated financial statements that are not included in this annual report, with the relevant adjustments due to the discontinued operations.

Income Statement Data:

	Year ended December 31,				
	2004	**2005**	**2006**	**2007**	**2008**
	(U.S. dollars in thousands, except share and per share data)				
Revenues:					
Software	$ 24,861	$ 21,503	$ 18,788	$ 17,707	$ 20,913
Maintenance and technical support	11,233	11,238	11,531	12,605	14,530
Consulting services	21,119	19,095	22,252	28,116	26,537
Total revenues	57,213	51,836	52,571	58,428	61,980
Cost of revenues:					

	Year ended December 31,				
Software	4,814	6,965	5,433	4,557	4,898
Maintenance and technical support	3,072	2,179	2,873	1,602	2,263
Consulting services	14,403	14,123	16,862	21,181	19,978
Total cost of revenues	22,289	23,267	25,168	27,340	27,139
Gross profit	34,924	28,569	27,403	31,088	34,841
Operating costs and expenses:					
Research and development, net	2,545	2,413	2,462	2,716	2,350
Selling and marketing	16,243	17,197	15,712	15,558	17,357
General and administrative	13,442	14,510	13,784	11,532	10,867
Restructuring and impairment	-	-	2,157	-	-
Operating income (loss)	2,694	(5,551)	(6,712)	1,282	4,267
Financial income (expense), net	917	(809)	332	161	448
Other income	-	-	278	170	-
Income (loss) before taxes on income	3,611	(6,360)	(6,102)	1,613	4,715
Taxes on income	254	462	310	362	199
Income (loss) after taxes on income	3,357	(6,822)	(6,412)	1,251	4,516
Equity in earnings (losses) of affiliates	79	19	15	(86)	(8)
Minority interest in losses (earnings) of subsidiaries	(67)	(8)	71	$ (22)	-
Net income (loss) from continued operations	$ 3,369	$ (6,811)	$ (6,326)	$ 1,143	$ 4,508
Net income from discontinued operations	721	2,204	1,320	11,465	-
Net income (loss)	4,090	(4,607)	(5,006)	12,608	4,508
Basic net income (loss) per share	$ 0.13	$ (0.15)	$ (0.16)	$ 0.40	$ 0.14
Diluted net income (loss) per share	$ 0.13	$ (0.15)	$ (0.16)	$ 0.39	$ 0.14
Shares used to compute basic income (loss) per share	31,029	31,124	31,184	31,443	31,769
Shares used to compute diluted income (loss) per share	32,426	31,124	31,184	32,023	32,032

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Balance Sheet Data:

	December 31,				
	2004	2005	2006	2007	2008
	(U.S. dollars in thousands)				
Working capital	$ 25,934	$ 19,052	$ 15,584	$ 28,737	$ 33,763
Cash, cash equivalents, short term deposits and marketable securities	10,982	10,173	11,653	16,446	32,588
Total assets including discontinued operations	80,285	73,722	71,172	82,298	82,656
Shareholders' equity	59,547	52,305	47,644	61,244	66,755

B. CAPITALIZATION AND INDEBTEDNESS

Not applicable.

C. REASONS FOR THE OFFER AND USE OF PROCEEDS

Not applicable.

D. RISK FACTORS

Investing in our ordinary shares involves a high degree of risk and uncertainty. You should carefully consider the risks and uncertainties described below before investing in our ordinary shares. Our business, prospects, financial condition and results of operations could be adversely affected due to any of the following risks. In that case, the value of our ordinary shares could decline, and you could lose all or part of your investment.

Risks Related to Our Business and Our Industry

We have a history of losses and may not be able to maintain profitability in the future.

Although we reported net income from continued operations of $ 1.1 million and $ 4.5 million for the years ended December 31, 2007 and 2008, respectively, we incurred losses in the two prior years. No assurance can be given that we will be able to maintain our current level of revenues or profitability in the future.

We have a history of quarterly fluctuations in our results of operations and expect these fluctuations to continue.

We have experienced and in the future may continue to experience significant fluctuations in our quarterly results of operations and we expect these fluctuations to continue. Factors that may contribute to fluctuations in our quarterly results of operations include:

The size and timing of orders;

The high level of competition that we encounter;

The timing of our product introductions or enhancements or those of our competitors or of providers of complementary products;

Market acceptance of our new products, applications and services;

The purchasing patterns and budget cycles of our customers and end-users;

The mix of product sales;

Exchange rate fluctuations; and

General economic conditions.

Our customers ordinarily require the delivery of products promptly after we accept their orders. With the exception of contracts for services, we usually do not have a backlog of orders for our products. Consequently, revenues from our products in any quarter depend on orders received and accepted by the customers in that quarter. The deferral of the placing and acceptance of any large order from one quarter to another could materially adversely affect our results of operations for the former quarter. Our customers sometimes require an acceptance test for services we provide and as a result, we may have a significant backlog of orders for our services. Our revenues from services depend on orders received and services provided by us and accepted by our customers in that quarter. If sales in any quarter do not increase correspondingly or if we do not reduce our expenses in response to level or declining revenues in a timely fashion, our financial results for that quarter would be materially adversely affected. For these reasons, quarter-to-quarter comparisons of our results of operations are not necessarily meaningful and you should not rely on the results of our operations in any particular quarter as an indication of future performance.

Continuing unfavorable national and global economic conditions could have a material adverse effect on our business, operating results and financial condition.

The recent crisis in the financial and credit markets in the United States, Europe and Asia has led to a global economic slowdown, with the economies of the United States and Europe showing significant signs of weakness. If the economies in any part of the world continue to be weak or weaken further, the demand for our products, technology and services may decrease as a result of continued constraints on capital spending by our customers. In addition, this could result in longer sales cycles, slower adoption of new technologies and increased price competition for our products and services. Any of these events would likely harm our business, operating results and financial condition. If global economic and market conditions, or economic conditions in the United States, Europe or Asia or other key markets, remain uncertain, persist, or deteriorate further, our business, operating results and financial condition may be materially adversely affected.

Recent worldwide economic downturn may adversely affect our customers, exposing us to credit risk and payment delinquencies on our accounts receivable.

Our outstanding accounts receivables are not covered by collateral. As economic conditions deteriorate, certain of our customers may face liquidity concerns and may delay or be unable to satisfy their payment obligations, which would have an adverse effect on our financial condition and operating results.

Changes in the ratio of our revenues generated from different revenue elements may adversely affect our gross profit margins.

We derive our revenues from the sale of software licenses, maintenance and technical support and consulting services. Our gross margin is affected by the proportion of our revenues generated from the sale of each of those elements of our revenues. Our revenues from the sale of our software licenses and maintenance and technical support have higher gross margins than our revenues from the sale of consulting services. If the relative proportion of our revenues from the sale of consulting services increases as a percentage of our total revenues, our gross profit margins will decline. Our software licenses revenues include the sale of the third party software license sales, which have a lower gross margin than the sales of our software products. Any increase in the portion of third party software license sales out of total license sales will decrease our gross profit margin.

We derive a significant portion of our revenues from independent distributors who are under no obligation to purchase our products and the loss of such independent distributors could adversely affect our business, results of operations and financial condition.

We sell our products through our direct sales representatives, as well as through third parties that use our technology to develop and sell solutions for their customers, referred to as ISVs or Magic Software Providors, or MSPs, and also through SIs. These independent distributors then resell our products to end-users. We are dependent upon the acceptance of our products by our independent distributors and their active marketing and sales efforts. Typically, our arrangements with our independent distributors do not require them to purchase specified amounts of products or prevent them from selling non-competitive products. The independent distributors may not continue, or may not give a high priority to, marketing and supporting our products. Our results of operations could be materially adversely affected by changes in the financial condition, business, marketing strategies, local and global economic conditions, or results of our independent distributors.

We may lose independent distributors on whom we currently depend and we may not succeed in developing new distribution channels which could adversely affect our business, results of operations and financial condition.

If any of our distribution relationships are terminated, we may not be successful in replacing them on a timely basis, or at all. In addition, we will need to develop new sales channels for new products, and we may not succeed in doing so. Any changes in our distribution and sales channels, or our inability to establish effective distribution and sales channels for new markets, will impact our ability to sell our products and result in a loss of revenues and profits.

We are dependent on a limited number of product families and a decrease in revenues from these products would adversely affect our business, results of operations and financial condition.

Currently, we derive most of our revenues from sales of application platform and integration products primarily under our uniPaaS and iBOLT brands, as well as related revenues from software maintenance and support and other services. We do not expect our revenue structure to change in the foreseeable future. Our future growth depends heavily on our ability to effectively develop and sell new and acquired products as well as add new features to existing products. A decrease in revenues from our primary products would adversely affect our business, results of operations and financial condition.

The revenue of one of our vertical subsidiaries is dependent upon two customers and a significant decrease in revenues from these customers could adversely affect our business, results of operations and financial condition.

The majority of revenues generated by one of our vertical subsidiaries in 2006, 2007 and 2008 were from two customers, and we expect the revenues of the subsidiary to continue to be largely dependent upon these two customers in 2009. We do not know if, or for how much longer, these two customers will continue to purchase the services of the subsidiary, nor do we have any control or influence over their purchasing decisions. A significant decrease in revenues from these customers could adversely affect our business, results of operations and financial condition.

Our widespread operations may strain our management, operational and financial resources and could have a material adverse affect on our business, results of operations and financial condition.

Our widespread operations have significantly strained our management, operational and financial resources in the past. Any future growth may increase this strain. To manage future growth effectively, we must:

- Expand our operational, management, financial, marketing and research and development functions;
- Train, motivate, manage and retain qualified employees; and
- Hire additional personnel.

We may not succeed in managing future growth.

We may encounter difficulties with our international operations and sales which could adversely affect our business, results of operations and financial condition.

While our principal executive offices are located in Israel, 92% of our sales in 2006, 2007 and 2008 were generated from other countries. This subjects us to many risks inherent to international business activities, including:

- Limitations and disruptions resulting from the imposition of government controls;
- Changes in regulatory requirements;
- Export license requirements;
- Economic or political instability;
- Trade restrictions;
- Changes in tariffs;
- Currency fluctuations;
- Difficulties in the collection of receivables;
- Foreign tax consequences;
- Greater difficulty in safeguarding intellectual property; and
- Difficulties in managing overseas subsidiaries and international operations.

We may encounter significant difficulties in connection with the sale of our products in international markets as a result of one or more of these factors and our business, results of operations and financial condition could be adversely affected.

Currency exchange rate fluctuations in the world markets in which we conduct business could have a material adverse affect on our business, results of operations and financial condition.

Our financial statements are stated in U.S. dollars, our functional currency. Nevertheless, a substantial portion of our revenues and expenses are incurred in other currencies, particularly Euros, Japanese yen, NIS and the British pound. We maintain substantial non-U.S. dollar balances of assets, including cash and accounts receivable, and liabilities, including accounts payable. Fluctuations in the value of the currencies in which we do business relative to the U.S. dollar may have a material adverse effect on our business, results of operations and financial condition, by decreasing the U.S. dollar value of assets held in other currencies and increasing the U.S. dollar amount of liabilities payable in other currencies, or by decreasing the U.S. dollar value of our revenues in other currencies and increasing the U.S. dollar amount of our expenses in other currencies. From time to time we use derivative or other instruments to hedge against part or all of our exposures.

Declines in our share price and/or operating performance could result in a future impairment of our goodwill or long-lived assets.

We assess potential impairments of goodwill annually and when there is evidence that events or changes in circumstances indicate that an impairment condition may exist. We assess potential impairments of our long-lived assets, including property and equipment and capitalized software, when there is evidence that events or changes in circumstances indicate that the carrying value may not be recoverable. In the current capital market downturn, our share price, and consequently our market capitalization, have declined and may decline further in the future. If the value of our market capitalization falls below the value of our shareholders equity, it might indicate that an impairment of goodwill is required. We determine the value of each of our reporting units using the income approach, which utilizes a discounted cash flow model, as we believe that this approach best approximates our fair value at this time. Our ability to reconcile the gap between our market capitalization and aggregate fair value of the reporting units depends on various factors, some of which are qualitative, such as estimated control premium that an investor would be willing to pay for a controlling interest in us, while others involve management judgment. If our market capitalization stays below our shareholders equity, or actual results of operations materially differ from our modeling estimates, we may be required to record a non-cash impairment charge of our goodwill. A significant impairment loss could have a material adverse effect on our operating results and on the carrying value of our goodwill and/or our long-lived assets on our balance sheet.

We face intense competition in the markets for our application platform as well as process and business integration technologies and services, which are evolving into a new market for software as a service, orSaaS. This competition could adversely affect our business, results of operations and financial condition.

We compete with other companies in the areas of application platforms, business integration and business process management, or BPM, tools, and in the applications and services markets in which we operate. The enhancement of the SaaS market increases the competition in these areas, and one of our competitors even claims to offer a fully automated eDeveloper conversion process, converting eDeveloper based applications to .NET based applications. We expect that competition will increase in the future, both with respect to our technology, applications and services which we currently offer and applications and services which we and other vendors are developing. Increased competition, direct and indirect, could adversely affect our business, financial condition and results of operations.

Some of our existing and potential competitors are larger, have substantially greater resources including financial, technological, marketing, skilled human resources and distribution capabilities, and enjoy greater market recognition than us. We may not be able to differentiate our products from those of our competitors, offer our products as part of integrated systems or solutions to the same extent as our competitors, or successfully develop or introduce new products that are more cost-effective, or offer better performance than our competitors. Failure to do so could adversely affect our business, financial condition and results of operations.

We may not succeed in increasing our market share in the business and process integration markets with our iBOLT products, or leverage our advantage in the rich internet application, or RIA, and SaaS enabled application platform, or SEAP, fields, which could adversely affect our business, results of operations and financial condition.

Our iBOLT Integration Suite provides business integration and process management solutions with a particular focus on enterprise applications. iBOLT allows the seamless integration and interoperability of diverse solutions, including legacy applications, in a quick and efficient manner. Since we launched iBOLT in 2003, we have continued to develop this product and enhance it, releasing successive versions over the years (the current version is 3.0). In 2005, we started a line of special editions of iBOLT tailored for specific application packages, and we have released three such special editions, for SAP, Oracle JD Edwards and Salesforce.com. We are currently developing solution accelerators, which will be periodically released during 2009.

The business integration and BPM markets in which we compete are extremely competitive and subject to rapid changes. Our competitors utilize varying approaches to the provision of technology to business integration and BPM markets. We may not have the resources, skills and product variety required to successfully increase our market share in these markets. In addition, even if we succeed in convincing prospective customers and the market that our products are effective and provide real business benefits, our target customers may not choose them due to technical, cost, support or other reasons.

Our future success will be largely dependent on the acceptance of future releases of our RIA and SEAP offerings and if we are unsuccessful our business, results of operations and financial condition will be adversely affected

In 2008, we released a new generation of our eDeveloper application platform, branded uniPaaS. uniPaaS is compatible with previous versions of eDeveloper, adds RIA capabilities, and in the future will add SaaS capabilities. Our future success will be in great measure dependent on the acceptance of uniPaaS. The acceptance of this product relies in part on the continued acceptance and growth of RIA and SaaS, for which uniPaaS is particularly useful and advantageous. If this product is not accepted, our business, results of operations and financial condition will be adversely affected.

Our efforts to increase our presence worldwide, including the United States, Europe, Japan, Asia, South Africa and Russia may not be profitable, which could adversely affect our business, results of operations and financial condition.

Our success in becoming a stronger competitor in the sale of application platform and integration solutions is dependent upon our ability to increase our sales in all our markets, including, but not limited to the United States, Europe, Japan, Asia Pacific, South Africa and Russia. Our efforts to increase our penetration to these markets are subject to risks inherent to such markets, including the high cost of doing business in such locations. Our efforts may be costly and the may not result in profits, which could adversely affect our business, results of operations and financial condition.

Rapid technological changes may adversely affect the market acceptance of our products and services, and our business, results of operations and financial condition could be adversely affected.

We compete in a market that is characterized by rapid technological change. The introduction of new technologies could render existing products and services obsolete and unmarketable and could exert price pressures on our products and services. Our future success will depend upon our ability to address the increasingly sophisticated needs of our customers by:

Supporting existing and emerging hardware, software, databases and networking platforms; and

Developing and introducing new and enhanced software development technology and applications that keeps pace with such technological developments, emerging new markets and changing customer requirements.

If release dates of any future products or enhancements are delayed or if, when released, they fail to achieve market acceptance, our business, financial condition and results of operations would be materially adversely affected.

Our products have a lengthy sales cycle which could adversely affect our revenues.

Our customers typically use our technology to develop and deploy as well as integrate applications that are critical to their businesses. As a result, the licensing and implementation of our technology generally involves a significant commitment of attention and resources by prospective customers. Because of the long approval process that typically accompanies strategic initiatives or capital expenditures by companies, our sales process is often delayed, with little or no control over any delays encountered by us. Our sales cycle can be further extended for sales made through third party distributors.

Our products may contain defects that may be costly to correct, delay market acceptance of our products and expose us to difficulties in the collection of receivables and to litigation.

Despite quality assurance testing performed by us, as well as by our partners and end-users who participate in our beta-testing programs, errors may be found in our software products or in applications developed with our technology. This risk is exacerbated by the fact that a significant percentage of the applications developed with our technology were and are likely to continue to be developed by our ISV partners and SIs over whom we exercise no supervision or control. If defects are discovered, we may not be able to successfully correct them in a timely manner or at all. Defects and failures in our products could result in a loss of, or delay in, market acceptance of our products, as well as difficulties in the collection of receivables and litigation, and could damage our reputation.

Our standard license agreement with our customers contains provisions designed to limit our exposure to potential product liability claims that may not be effective or enforceable under the laws of some jurisdictions. Accordingly, we could fail to realize revenues and suffer damage to our reputation as a result of, or in defense of, a substantial claim.

Our proprietary technology is difficult to protect and unauthorized use of our proprietary technology by third parties may impair our ability to compete effectively.

Our success and ability to compete depend in large part upon our ability to protect our proprietary technology. We rely on a combination of trade secret and copyright laws and confidentiality, non-disclosure and assignment-of-inventions agreements to protect our proprietary technology. We do not have any patents. Our policy is to require employees and consultants to execute confidentiality agreements upon the commencement of their relationships with us. These measures may not be adequate to protect our technology from third-party infringement, and our competitors might independently develop technologies that are substantially equivalent or superior to ours. Additionally, our products may be sold in foreign countries that provide less protection for intellectual property rights than that provided under U.S. or Israeli laws.

Third parties may claim that we infringe upon their intellectual property rights and could harm our business.

Third parties may assert infringement claims against us or claims that we have violated a patent or infringed upon a copyright, trademark or other proprietary right belonging to them. Any infringement claim, even one without merit, could result in the expenditure of significant financial and managerial resources to defend any such claims.

We may be unable to attract, train and retain qualified personnel, which could adversely affect our business, results of operations and financial condition.

In the event our business grows, we will need to hire additional qualified personnel. The process of locating, training and successfully integrating qualified personnel into our operations can be lengthy and expensive. We may not be able to attract the personnel we need. Any loss of members of senior management or key technical personnel, or any failure to attract or retain highly qualified employees as needed, could have a material adverse effect on our business, financial condition and results of operations.

We made and expect to make acquisitions that could disrupt our operations and harm our operating results.

Our growth depends upon market growth, our ability to enhance our existing products, and our ability to introduce new products on a timely basis. We intend to continue to address the need to develop new products and enhance existing products through acquisitions of other companies, product lines, technologies, and personnel. Acquisitions involve numerous risks, including the following:

Difficulties in integrating the operations, systems, technologies, products, and personnel of the acquired companies;

Diversion of management s attention from normal daily operations of the business and the challenges of managing larger and more widespread operations resulting from acquisitions;

Potential difficulties in completing projects associated with in-process research and development;

Difficulties in entering markets in which we have no or limited direct prior experience and where competitors in such markets have stronger market positions;

Initial dependence on unfamiliar supply chains or relatively small supply partners;

Insufficient revenue to offset increased expenses associated with acquisitions; and

The potential loss of key employees, customers, distributors, vendors and other business partners of the companies we acquire following and continuing after announcement of acquisition plans.

Mergers and acquisitions of high-technology companies are inherently risky and subject to many factors outside of our control and no assurance can be given that our future acquisitions will be successful and will not materially adversely affect our business, operating results, or financial condition. Failure to manage and successfully integrate acquisitions could materially harm our business and operating results. Prior acquisitions have resulted in a wide range of outcomes, from successful introduction of new products and technologies to a failure to do so. Even when an acquired company has already developed and marketed products, there can be no assurance that product enhancements will be made in a timely fashion or that pre-acquisition due diligence will have identified all possible issues that might arise with respect to such products.

Because we are controlled by Formula Systems (1985) Ltd. and Emblaze Ltd., investors will not be able to affect the outcome of shareholder votes.

Formula Systems (1985) Ltd., or Formula Systems, an Israeli company whose shares trade on the NASDAQ Global Market and the Tel Aviv Stock Exchange, or TASE, directly owns 18,560,352, or 58.2%, of our outstanding ordinary shares. Emblaze Ltd., or Emblaze, an Israeli company traded on the London Stock Exchange, owns 51.7% of the outstanding shares of Formula Systems. Although transactions between us and our controlling shareholders are subject to special approvals under Israeli law (see Item 6C. Directors, Senior Management and Employees Board Practices Disclosure of Personal Interests of a Controlling Shareholder; Approval of Transactions with Controlling Shareholders), Formula Systems and Emblaze will be able to exercise control over our operations and business strategy and affairs, including any determinations with respect to potential mergers or other business combinations involving us, our acquisition or disposition of assets, our incurrence of indebtedness, our issuance of any additional ordinary shares or other equity securities, our repurchase or redemption of ordinary shares and our payment of dividends. Similarly, Formula Systems and Emblaze will be able to control most matters requiring shareholder approval, including the election of our directors (subject to a special majority required for the election of outside directors). Such concentration of ownership may have the effect of delaying or preventing an acquisition or a change in control of us.

If we are unable to maintain effective internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act of 2002, the reliability of our financial statements may be questioned and our share price may suffer.

The Sarbanes-Oxley Act of 2002 imposes certain duties on us and on our executives and directors. Our efforts to comply with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 governing internal control and procedures for financial reporting, which started in connection with our 2007 Annual Report on Form 20-F, have resulted in increased general and administrative expense and a diversion of management time and attention, and we expect these efforts to require the continued commitment of significant resources. We may identify material weaknesses or significant deficiencies in our assessments of our internal controls over financial reporting. Failure to maintain effective internal control over financial reporting could result in investigation or sanctions by regulatory authorities, and could have a material adverse effect on our operating results, investor confidence in our reported financial information and the market price of our ordinary shares.

Risks Related to Our Ordinary Shares

Our share price has been very volatile in the past and may continue to be susceptible to significant market price and volume fluctuations in the future.

Our ordinary shares have experienced significant market price and volume fluctuations in the past and may experience significant market price and volume fluctuations in the future in response to factors such as the following, some of which are beyond our control:

Quarterly variations in our operating results;

Changes in expectations as to our future financial performance, including financial estimates by securities analysts and investors;

Announcements of technological innovations or new products by us or our competitors;

Announcements by us or our competitors of significant contracts, acquisitions, strategic partnerships, joint ventures or capital commitments;

Changes in the status of our intellectual property rights;

Announcements by third parties of significant claims or proceedings against us;

Additions or departures of key personnel;

The public s response to our press releases, our other public announcements and our filings with the Securities and Exchange Commission and the Israeli Securities Authority;

Future sales of our ordinary shares by our directors, officers and significant shareholders;

Political and economic conditions, such as a recession or interest rate or currency rate fluctuations or political events;

Other events or factors in any of the countries in which we operate, including those resulting from war, incidents of terrorism, natural disasters or responses to such events; and

General trends of the stock markets.

Domestic and international stock markets often experience extreme price and volume fluctuations. The market prices of ordinary shares of software companies have been extremely volatile. Stock prices of many software companies have often fluctuated in a manner unrelated or disproportionate to the operating performance of such companies. In the past, securities class action litigation has often been brought against registrants following periods of volatility in the market price of their securities. We may in the future be the targets of similar litigation. Securities litigation could result in substantial costs and divert management s attention and resources.

We have not paid any cash dividends on our ordinary shares in the last five fiscal years and may not do so in the future.

Although we paid a dividend in 2003 we did not pay any cash dividends on our ordinary shares in the last five fiscal years. Future dividend distributions are subject to the discretion of our board of directors and will depend on various factors, including our operating results, future earnings, capital requirements, financial condition and tax implications of dividend distributions on our income, future prospects and any other factors deemed relevant by our board of directors. The distribution of dividends also may be limited by Israeli law, which permits the distribution of dividends only out of profits (as defined by Israeli law) or otherwise upon the permission of the court. You should not rely on an investment in our company if you require dividend income from your investment. The success of your investment will likely depend entirely upon any future appreciation of the market price of our ordinary shares, which is uncertain and unpredictable. There is no guarantee that our ordinary shares will appreciate in value or even maintain the price at which you purchased your ordinary shares.

Our ordinary shares are traded on more than one market and this may result in price variations.

Our ordinary shares are traded primarily on the NASDAQ Global Market and on the Tel Aviv Stock Exchange. Trading in our ordinary shares on these markets is made in different currencies (U.S. dollars on the NASDAQ Global Market, and New Israeli Shekels, or NIS, on the Tel Aviv Stock Exchange), and at different times (resulting from different time zones, different trading days and different public holidays in the United States and Israel). Consequently, the trading prices of our ordinary shares on these two markets may differ. Any decrease in the trading price of our ordinary shares on one of these markets could cause a decrease in the trading price of our ordinary shares on the other market.

Risks Related to Our Location in Israel

Political, economic and military instability in Israel may disrupt our operations and negatively affect our business condition, harm our results of operations and adversely affect our share price.

We are incorporated under the laws of, and our executive offices and research and development facilities are located in, the State of Israel. Although most of our sales are made to customers outside Israel, we are influenced to a limited extent by the political, economic and military conditions affecting Israel. Specifically, we could be adversely affected by any major hostilities involving Israel, the interruption or curtailment of trade between Israel and its present trading partners, or a significant downturn in the economic or financial condition of Israel.

Since the establishment of the State of Israel in 1948, Israel and its Arab neighbors have engaged in a number of armed conflicts. A state of hostility, varying from time to time in intensity and degree, has led to security and economic problems for Israel. Major hostilities between Israel and its neighbors may hinder Israel s international trade and lead to economic downturn. This, in turn, could have a material adverse effect on our operations and business. There has been an increase in unrest and terrorist activity in Israel, which began in September 2000 and which continued with varying levels of severity through 2008. The future effect of this deterioration and violence on the Israeli economy and our operations is unclear. In the summer of 2006, Israel was engaged in an armed conflict with Hezbollah, which involved missile strikes against civilian targets in northern Israel and negatively affected business conditions in Israel. The establishment in 2006 of a government in the Gaza Strip by representatives of the Hamas, which effectively took control of the Gaza Strip from the Palestinian Authority in 2007 following Israel s disengagement from the Gaza Strip in 2005, has created additional unrest and uncertainty in the region. In December 2008 and January 2009, there was an armed conflict between Israel and Hamas, following the firing of thousands of missile into southern Israel. The missile attacks by Hamas have not targeted the greater Tel Aviv region, the location of our principal executive offices; however, any armed conflicts, terrorist activities or political instability in the region would likely negatively affect business conditions and could significantly harm our results of operations.

Furthermore, there are a number of countries, primarily in the Middle East, as well as Malaysia and Indonesia, that restrict business with Israel or Israeli companies, and we are precluded from marketing our products to these countries. Restrictive laws or policies directed towards Israel or Israeli businesses may have an adverse impact on our operations, our financial results or the expansion of our business.

Our results of operations may be negatively affected by the obligation of our personnel to perform military service.

Many of our executive officers and employees in Israel are obligated to perform annual reserve duty in the Israeli Defense Forces and may be called for active duty under emergency circumstances at any time. If a military conflict or war arises, these individuals could be required to serve in the military for extended periods of time. Our operations could be disrupted by the absence for a significant period of one or more of our executive officers or key employees or a significant number of other employees due to military service. Any disruption in our operations could adversely affect our business.

Our financial results may be adversely affected by inflation and currency fluctuations.

We report our financial results in dollars, while a substantial portion of our expenses, primarily labor expenses, are incurred in NIS. Therefore, our NIS related costs, as expressed in U.S. dollars, are influenced by the exchange rate between the U.S. dollar and the NIS. During 2007 and 2008, the NIS appreciated against the U.S. dollar, which resulted in a significant increase in the U.S. dollar cost of our NIS expenses. We are also influenced by the timing of, and the extent to which, any increase in the rate of inflation in Israel over the rate of inflation in the United States is not offset by the devaluation of the NIS in relation to the dollar. Our dollar costs in Israel will increase if inflation in Israel exceeds the devaluation of the NIS against the U.S. dollar or if the timing of such devaluation lags behind inflation in Israel. We cannot predict any future trends in the rate of inflation in Israel or the rate of devaluation or appreciation of the NIS against the dollar. If the dollar cost of our operations in Israel increases, our dollar measured results of operations will be adversely affected.

We currently have the ability to benefit from government tax benefits, which may be cancelled or reduced in the future.

We are eligible to receive tax benefits under Government of Israel programs. In order to maintain our eligibility for these tax benefits, we must continue to meet specific conditions. If we fail to comply with these conditions in the future, the tax benefits we could receive may be cancelled.

Service and enforcement of legal process on us and our directors and officers may be difficult to obtain.

We are incorporated in Israel and some of our directors, executive officers and the Israeli experts named in this annual report reside outside the United States. Service of process upon them may be difficult to effect within the United States. Furthermore, most of our assets and the assets of some of our executive officers and directors and some of the experts named in this annual report are located outside the United States. Therefore, a judgment obtained against us or any of them in the United States, including one based on the civil liability provisions of the U.S. federal securities laws may not be collectible in the United States and may not be enforced by an Israeli court. It also may be difficult for you to assert U.S. securities law claims in original actions instituted in Israel. For more information regarding the enforceability of civil liabilities against us, our directors and executive officers and the Israeli experts named in this prospectus, including the terms under which certain judgments may be enforced by an Israeli court, please see Enforceability of Civil Liabilities.

Provisions of Israeli law may delay, prevent or make difficult an acquisition of us, which could prevent a change of control and therefore depress the price of our shares.

Israeli corporate law regulates mergers, requires tender offers for acquisitions of shares above specified thresholds, requires special approvals for transactions involving directors, officers or significant shareholders and regulates other matters that may be relevant to these types of transactions. Furthermore, Israeli tax considerations may make potential transactions unappealing to us or to some of our shareholders. These provisions of Israeli corporate and tax law may have the effect of delaying, preventing or complicating a merger with, or other acquisition of, us. This could cause our ordinary shares to trade at prices below the price for which third parties might be willing to pay to gain control of us. Third parties who are otherwise willing to pay a premium over prevailing market prices to gain control of us may be unable or unwilling to do so because of these provisions of Israeli law.

Your rights and responsibilities as a shareholder will be governed by Israeli law and differ in some respects from the rights and responsibilities of shareholders under U.S. law.

We are incorporated under Israeli law. The rights and responsibilities of holders of our ordinary shares are governed by our memorandum of association, articles of association and by Israeli law. These rights and responsibilities differ in some respects from the rights and responsibilities of shareholders in typical U.S. corporations. In particular, a shareholder of an Israeli company has a duty to act in good faith in exercising his or her rights and fulfilling his or her obligations toward the company and other shareholders and to refrain from abusing his power in the company, including, among other things, in voting at the general meeting of shareholders on certain matters. Israeli law provides that these duties are applicable in shareholder votes at the general meeting with respect to, among other things, amendments to a company s articles of association, increases in a company s authorized share capital, mergers and actions and transactions involving interests of officers, directors or other interested parties which require the shareholders general meeting s approval. In addition, a controlling shareholder of an Israeli company or a shareholder who knows that he or she possesses the power to determine the outcome of a vote at a meeting of our shareholders, or who has, by virtue of the company s articles of association, the power to appoint or prevent the appointment of an office holder in the company, or any other power with respect to the company, has a duty of fairness toward the company. The Israeli Companies Law does not establish criteria for determining whether or not a shareholder has acted in good faith. Moreover, the law is relatively new and there is no case law available on the duty of a non-controlling shareholder to act in good faith.

As a foreign private issuer whose shares are listed on the NASDAQ Global Market, we may follow certain home country corporate governance practices instead of certain NASDAQ requirements. We follow Israeli law and practice instead of NASDAQ rules regarding the requirement that our independent directors have regularly scheduled meetings at which only independent directors are present.

As a foreign private issuer whose shares are listed on The NASDAQ Global Market, we are permitted to follow certain home country corporate governance practices instead of certain requirements of the NASDAQ Marketplace Rules. We follow Israeli law and practice instead of The NASDAQ Marketplace Rules regarding the requirement that our independent directors have regularly scheduled meetings at which only independent directors are present. As a foreign private issuer listed on the NASDAQ Global Market, we may also follow home country practice with regard to, among other things, the composition of the board of directors, director nomination procedure, compensation of officers and quorum at shareholders meetings. In addition, we may follow our home country law, instead of the NASDAQ Marketplace Rules, which require that we obtain shareholder approval for certain dilutive events, such as for the establishment or amendment of certain equity based compensation plans, an issuance that will result in a change of control of the company, certain transactions other than a public offering involving issuances of a 20% or more interest in the company and certain acquisitions of the stock or assets of another company. A foreign private issuer that elects to follow a home country practice instead of such requirements must submit to NASDAQ in advance a written statement from an independent counsel in such issuer s home country certifying that the issuer s practices are not prohibited by the home country s laws. In addition, a foreign private issuer must disclose in its annual reports filed with the Securities and Exchange Commission each such requirement that it does not follow and describe the home country practice followed by the issuer instead of any such requirement. Accordingly, our shareholders may not be afforded the same protection as provided under NASDAQ s corporate governance rules.

ITEM 4. INFORMATION ON THE COMPANY

A. HISTORY AND DEVELOPMENT OF THE COMPANY

We were incorporated under the laws of the State of Israel in February 1983 as Mashov Software Export (1983) Ltd. and we changed our name to Magic Software Enterprises Ltd. in 1991. We are a public limited liability company and operate under the Israeli Companies Law 1999 and associated legislation. Our registered offices and principal place of business are located at 5 Haplada Street, Or Yehuda 60218, Israel, and our telephone number is +972-3-538-9292. Our U.S. subsidiary, Magic Software Enterprises Inc., is located at 23046 Avenida de la Carlota, Laguna Hills, CA 926653. Our address on the Internet is www.magicsoftware.com. The information on our website is not incorporated by reference into this annual report.

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We develop, market and support uniPaaS, an application platform for software development and deployment, and iBOLT, a platform for business integration and BPM. The uniPaaS and the iBOLT enable enterprises to accelerate the process of building and deploying applications that can be rapidly customized and integrated with existing systems.

As a leading IT technology innovator, we have over 25 years of experience in assisting software companies and enterprise software companies worldwide to produce and integrate their business applications. Our application platform, uniPaaS, is used by thousands of enterprises and ISVs to develop solutions for their customers in approximately 50 countries. We also refer to these ISVs as MSPs. We also provide maintenance and technical support as well as professional services to our enterprise customers and to MSPs. In addition, we sell our technology for business integration, iBOLT, to customers of specific popular software applications, such as SAP, Salesforce.com, IBM i (AS/400) or Oracle JD Edwards or other business applications. We refer to these vendor-centered market sectors as ecosystems.

In May 2008, we launched the uniPaaS application platform, the next generation of our eDeveloper. In July 2008, uniPaaS was made available worldwide. Since May 2008, we have introduced a strategy to improve the penetration of our uniPaaS application platform by organizing user-group events, globally. In November 2008, we released the latest version of our flagship application platform, uniPaaS V1.5 for developing RIAs.

In 2008, we developed a migration program consisting of special prices, training marketing campaigns and informative webinars to help our customers achieve a smooth migration to new RIA technologies.

In 2008, we sharpened our iBOLT business integration suite to focus more on gaining ecosystem business. We have recruited a number of new partners from within a number of various ecosystems and gained new partners to aid our sales for both uniPaaS and iBOLT. To support this we ve increased our attendance at major ecosystem events in 2008.

In the latter part of 2008, we released a controlled and limited first version of iBOLT Version 3. Since then we have continued to develop the iBOLT channel and have entered into agreements with additional SIs, consultancies and service providers who acquired iBOLT skills and offer iBOLT licenses and related services to their customers.

In May 2008, we launched our partnership with Salesforce.com, an on-demand customer relationship management, or CRM, solution vendor, and introduced iBOLT Special Edition for Salesforce.com integration solution. Since then we have developed partnerships with SIs in the Salesforce.com ecosystem and we are continuing to experience increasing sales in this sector.

In June 2008, we introduced the new Intercompany Accelerator as part of the iBOLT for SAP solution. In July 2008, we won the SAP Business One Global Solution Partner Award for Leadership in Innovation. This is the third consecutive year that we have won a SAP partner award.

In the last quarter of 2008, we focused the iBOLT integration tool on the SAP R/3 market, and to date we completed several successful new deployments of iBOLT for SAP ERP R3.

We have increased our penetration into the JD Edwards market, particularly in the United States where we have gained a number of new partners specializing in JD Edwards solutions and won a number of significant deals.

We have continued to work closely with IBM as an Advanced Partner of the IBM Partnerworld for Developer Business Partner program and as a Member Partner of IBM Partnerworld for Software. IBM has awarded us with its ServerProven® certification for our uniPaaS and iBOLT products following a rigorous testing and evaluation process. Only those products that are validated by IBM to install quickly, start up easily and run reliably on IBM servers are awarded this certification, designed by IBM to assist its customers to easily identify complete solutions for their business-critical e-business needs. We are also part of IBM s System i Tools Innovation Program. As part of our activities with the IBM i customers and business partners, we released a special edition of iBOLT for Oracle JD Edwards, targeted at users of JD Edwards Enterprise One Oracle enterprise resource planning, or ERP, software on the IBM System i platform.

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On December 30, 2007, we sold our wholly-owned subsidiary, Advanced Answers on Demand Holding Corporation, or AAOD, a Florida corporation that develops and markets application software targeted at the long-term care industry, to Fortissimo Capital, for $17 million. Fortissimo Capital paid us $1.0 million of the sale price in December 2007 and the remaining $16 million at the beginning of 2008. In addition, as part of the transaction, we entered into a three year license agreement with AAOD according to which AAOD will continue to sell products based on our platform in consideration of $3.0 million, to be paid quarterly over three years starting in 2008. We recorded a capital gain of $9.3 million in discontinued operations as a result of the transaction in 2007.

In June 2008, we sold our 40% interest in Nextstep Infotech PVT. Ltd., or Nexstep, in consideration of $150,000. We recorded a capital loss of $61,000 as a result of the transaction in 2008.

Our capital expenditures for the years ended December 31, 2006, 2007 and 2008 were approximately $1.0 million, $0.8 million and $0.7 million, respectively. These expenditures were principally for network equipment and computers, furniture and office equipment and leasehold improvements.

B. BUSINESS OVERVIEW

Industry Overview

In recent years the multiplication of enterprise applications has lead to a level of complexity of an enterprise s information system that is obstructing business progress and evolution, reducing business agility and often resulting in multiple versions of similar data objects, such as customer records. We believe that one of the main challenges the modern enterprise faces today is creating a single view of the truth, which is the better way to make effective and relevant business decisions. Business integration is employed to facilitate this. Traditionally, given their cost and complexity, business integration solutions were targeted at large enterprises. Consequently, business integration tools are mostly complex, require significant implementation resources, take a long time to implement and are costly. Given the critical need for business integration across the demand and supply chain, enterprises of all sizes require such solutions. We recognized this trend and emerging need when we designed iBOLT.

Another major evolution in enterprises is the trend of reusing IT assets, such as enterprise applications, which is driving the move towards service oriented architecture, or SOA. Due to the large investments in enterprise applications, such as ERP and CRM, on the one hand, and the accelerating business change, on the other hand, organizations need to find a way to continue to leverage and amortize their IT investments while increasing their ability to change business processes and support new ones. The software industry s response is a new SOA, a new paradigm of application development, service oriented development architecture, and composite applications. Most of these involve metadata (which is data that describes other data, similar to a table of content describing a book), rather than traditional programming. We have developed and enhanced this paradigm over the last 20 years, and we believe that we have one of the largest installed-base of products employing such technology.

Additionally, SaaS is becoming a well-established phenomenon in some areas of enterprise IT. It is growing into a mainstream option for software-based business solutions and will affect most of enterprise IT departments in the next three years in one way or another. It appears that SEAP is becoming a dominant player in the growing SaaS application industry. We are developing our technology to provide the functionality of a SEAP, as a result of the growing demand from application vendors to repackage their applications as a SaaS offering. In 2008, we were already recognized by independent industry analysts such a Gartner as one of the few vendors, providing a comprehensive application platform for SaaS and cloud computing.

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General

Our technology enables enterprises to accelerate the process of building and deploying business software applications that can be rapidly customized to meet current and future needs. Our development and integration products empower customers to dramatically improve their business performance and return on investment by enabling the affordable and rapid integration of diverse applications, systems and databases to streamline business processes from within one comprehensive framework.

Our technology and solutions are especially in demand when time-to-market considerations are critical, budgets are tight, integration is required with multiple platforms or applications, databases or existing systems and business processes, as well as for RIA, cloud computing and SaaS.

We address the critical business needs of companies so that they are able to quickly respond to changing market forces and demands. Robust business solutions are created, deployed and maintained with unrivaled productivity and time-to-market results. Our development paradigm is aligned with modern application development theories and enables developers to create better solutions in less time and with fewer resources.

Our technology, comprised of the iBOLT and uniPaaS solutions, is comprehensive and industry proven. These technologies can be applied to the entire software development market, from the implementation of micro-vertical solutions, through tactical application renovation and process automation solutions, to enterprise spanning SOA migrations and composite applications initiatives. Unlike most competing platforms, we offer a coherent and unified toolset stemming from the same proven metadata driven and rules based declarative technology, resulting in unprecedented cost savings through fast and easy implementation and reduced project risk.

Development communities are facing high complexity, cost and extended pay-back periods in order to deliver SaaS applications. uniPaaS and iBOLT provide ISV s with the ability to rapidly build integrated applications in a more productive manner, deploy them in multiple modes and architectures as needed, lower IT maintenance costs and decreasing time-to-market.

With the launch of iBOLT, we started a process of expanding from the application development field to the business integration and process management fields, which are, presently converging, from a technology perspective, to the composite application field. Products for these fields require SOA, application integration capabilities, process management, orchestration capabilities, and information delivery capabilities. Our technology and products provide all of these capabilities.

With the impending introduction of our SEAP, we expect to strengthen our position as a leading application platform provider opening the path for us to address the top-tier sector of the market. The increasing adoption of the SaaS delivery and business model requires the use of a new generation application platforms, which support the relevant functions required for SaaS deployment. We are one of the first vendors to offer such a platform. By leveraging the easy migration of applications between the different versions of our products, our MSPs have the potential to become among the first and most versatile sources of SaaS applications. Industry analysts as well as several of our major MSPs have recognized this, and we have begun to work with some of them in this context.

Our Products

The driving principles behind our technology are:

Focus on business logic rather than technological means using our tried and tested code-free approach;

Abstraction - to hide complexity and facilitate change;

Automation of mundane tasks - to accelerate development and maintenance and reduce risk; and

Interoperability to support business logic across multiple hardware and software platforms, operating systems and geographies.

We offer two complementary products that address the wide spectrum of composite applications.

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uniPaaS Application Platform

The uniPaaS application platform was released during 2008 as the next generation of eDeveloper. uniPaaS was released in recognition of the growing market demand for RIA and SaaS. It features new functionality and extensions to our application platform, with the objective of enabling the development of RIA and SaaS applications. SaaS is a relatively new business and technical model for delivering software applications, similar to a phone or cable TV model, in which the software applications are installed and operated in dedicated data centers and users subscribe to these centers and use the applications over an internet connection. This model requires the ability to deliver RIA.

uniPaaS is a comprehensive RIA platform which is also cloud enabled. It is the industry s first RIA and SEAP that uses a single development paradigm to handle all client and server partitioning. uniPaaS offers customers the power to choose how they deploy their applications, whether full client or web; on-premise or on-demand; in the cloud or behind the corporate firewall; software or SaaS; and global or local. Our uniPaaS application platform complies with event driven and service oriented architectural principles. By offering technology transparency, this product allows customers focus on their business requirements rather than technological means. uniPaaS single development paradigm significantly reduces the time and costs associated with the development and deployment of RIAs. In addition, application owners can leverage their initial investment when moving from full client mode to RIA and SaaS, and eventually modify these choices as the situation requires. Furthermore, enterprises can use cloud based uniPaaS applications in a SaaS model and still have their databases in the privacy of their own data centers. It also supports most hardware and operating system environments such as Windows, Unix, Linux and AS/400, as well as multiple databases. In addition, uniPaas is interoperable with .NET and Java technologies.

uniPaaS can be applied to the full range of software development, from the implementation of micro-vertical solutions, through tactical application renovation and process automation solutions, to enterprise spanning SOA migrations and composite applications initiatives. Unlike most competing platforms, we offer a coherent and unified toolset stemming from the same proven metadata driven and rules based declarative technology, resulting in unprecedented cost savings through fast and easy implementation and reduced project risk.

iBOLT Business and Process Integration

The iBOLT business integration suite is a graphical, wizard-based code-free solution delivering fast and simple integration and orchestration of business processes and applications. iBOLT allows businesses to more easily view, access, and leverage their mission-critical information, delivering true enterprise application integration, or EAI, BPM, and SOA, infrastructure.

iBOLT allows the seamless integration and interoperability of diverse solutions, including legacy applications, in a quick and efficient manner. In 2008, we released iBOLT Version 3.0 and since then we have continued to develop the iBOLT channel and entered into agreements with additional SIs, consultancies and service providers, who acquired iBOLT skills and offer iBOLT licenses and related services to their customers.

Increasing the usability and life span of existing legacy and other IT systems, iBOLT allows fast EAI, development and customization of diverse applications, systems and databases, assuring rapid return on invested capital and time-to-market, increased profitability, and customer satisfaction. We also offer special editions of iBOLT targeted at specific enterprise application vendor ecosystems, such as SAP, JD Edwards or Salesforce.com. These special editions contain specific features and pricing tailored for these market sectors.

Our Value Proposition

Our technology and solutions are especially in demand when budgets are tight and time-to-market considerations are critical. Our technology enables enterprises to accelerate the process of building and deploying business software applications that can be rapidly customized to meet current and future needs. Our development and integration products empower customers to dramatically improve their business performance and return on investment by enabling the affordable and rapid integration of diverse applications, systems and databases to streamline business processes from within one comprehensive framework.

We address the critical business needs of companies so that they are able to quickly respond to changing market forces and demands. Robust business solutions are created, deployed and maintained with unrivaled productivity and time-to-market results.

With uniPaaS, our unique, single development paradigm is aligned with modern application development theories and enables developers to create better solutions in less time and with fewer resources.

uniPaaS offers our customers ISVs, SIs and enterprises the following benefits:

Time to Market. uniPaaS eliminates the difficulties and costs of developing distinct client and server paradigms and partitioning.

Total Cost of Ownership. When deployment is required uniPaaS automatically instructs the business logic to the various technical components, thus saving the need for human intervention or planning and enabling deployment at an unprecedented low cost of ownership.

Deployment Flexibility. Unique to the market, uniPaaS gives users the power to choose how they deploy their applications, whether full client or web, on-premise or on-demand, software or SaaS.

Scalability and Adaptability. uniPaaS enables application owners to move from full client mode to RIA and SaaS and back again as business situations and demands change.

Portability. uniPaaS can be used with most hardware platforms, operating systems and databases. Applications developed with our technology for one platform can also be deployed on other supported platforms.

Database Access and Technology Independence. Our technology can easily move data across platforms and convert the data from one database format to another.

Comprehensiveness. uniPaaS incorporates all aspects of the development and deployment process which usually requires organizations to buy and integrate multiple and diverse Server and Client paradigms.

Global Experience and Expertise. uniPaaS leverages 25 years of research and development, including applied customer experience and feedback.

We believe that iBOLT offers our customers and partners the following benefits:

Time to Market. iBOLT has services, components and wizards that translate into a level of productivity between five and ten times greater than other technologies, ensuring that once an integration project is started, it finishes on time and on budget.

Cost Effectiveness. Many vendors design their business logic in a way that s so complex; customers can barely use it. iBOLT s graphical business flow editor allows users to easily and intuitively configure their business processes, ensuring that their end project is practical, usable and gives value for their money.

Comprehensiveness. iBOLT is a comprehensive integration technology stack, guaranteeing powerful and cost-effective integration for any business scenario.

Deployment Flexibility. iBOLT has a significant range of built-in certified and optimized adaptors to maximize the integration flexibility and intuitive use.

Scalability and Adaptability. iBOLT is used by hundreds of companies of every size in every vertical worldwide and is responsible for tens of millions of transactions every single day.

Global Experience and Expertise. iBOLT leverages 25 years of research and development, including applied customer experience and feedback. uniPaaS stands at the core of the iBOLT integration suite, from studio to its actual deployment.

Special editions of iBOLT with optimized adaptors are available to expand the capabilities of the most commonly used ERP and CRM packages, including SAP Business One, SAP Business All-in-One, SAP R/3, Salesforce.com, JD Edwards, IBM i Series, Lotus Notes, and HL7.

Our Strategy

Our goal is to achieve a leadership position in the application platform and business integration markets. We focus on providing technology, applications and services that enable enterprises to meet their business needs on time and budget. The key elements of our strategy to achieve this goal are to:

Develop and up-sell to our installed base and partner community by leveraging our solutions (uniPaaS, iBOLT and professional services);

Utilize connectivity/integration solutions (iBOLT based) in existing ecosystems (SAP, Salesforce.com, JD Edwards and OEMs) to enlarge our installed base;

Strengthen our alliance with SAP, Salesforce.com, Oracle JD Edwards and IBM i;

Develop additional alliances with leading application vendors and develop offerings and partner programs for their ecosystems, such as Oracle s JD Edwards and Salesforce.com;

Focus on recruiting OEM partners that will incorporate our iBOLT integration technology into their product offerings;

Promote uniPaaS (RIA and SaaS platforms) into the mid- and upper-markets of both enterprises and ISVs;

Increase the number of software houses and ISVs that use uniPaaS to build their applications;

Focus our sales efforts on our core products, uniPaaS and iBOLT; and

Focus our efforts on further building a strong partner base of SIs, ISVs, distributors, resellers, OEMs and consulting partners of our core technologies.

Product Development

The software industry is characterized by rapid technological changes and is highly competitive with respect to timely product innovation. We must maintain compatibility and competitiveness in the face of ongoing changes in industry standards.

We place considerable emphasis on research and development in order to improve and expand the functionality of our technology and to develop new applications. We believe that our future success depends upon our ability to maintain our technological leadership, to enhance our existing products and to introduce new commercially viable products addressing the needs of our customers on a timely basis. We also intend to support emerging technologies as they are introduced in the same way we have supported new technologies in the past. We will continue to devote a significant portion of our resources to research and development. We believe that internal development of our technology is the most effective means of achieving our strategic objective of providing an extensive, integrated and feature-rich development technology.

During 2008, we invested mainly in the development of the following products:

uniPaaS. During 2008, in response to customers needs and service requests, we released uniPaaS version 1.0 and later version 1.5, as well as service packs for current eDeveloper versions.

RIA Technology. This is a new technology of web based solutions. Based on eDeveloper browser client engine, we developed a new client module that provides full thin-client functionality using standard widgets. The advantage of the new technology is its ability to run on any .NET device, significantly reducing the cost of application management and operation. We are continuing to develop the technology targeting the SaaS market. We plan to release a version of uniPaaS with full SaaS capabilities during the first half of 2009.

A new version of iBOLT. iBOLT Version 3 was the main focus of the iBOLT development in 2008. The new version delivers a full range of new functionalities for the integration market as well as massive performance improvements. Some of the main functionalities include new data mapper, expression editor, user defined storages, resource management and component software development kit.

Intercompany iBOLT solution. In 2007 we developed a generic solution for inter-company synchronization with iBOLT Version 2.5. Some of the main functionalities include mail and HTTP synchronization, object management, synchronization process monitoring and more. We released the first version during the fourth quarter of 2007 and continue to improve the functionality of this product.

Hermes software. In 2007, we continued to develop the Hermes software solution for air cargo handling. HERMES Releases 3.1 and 3.2 incorporate new and advanced functionalities. HERMES Release 3.1 software is operating in full production. During 2008, HERMES Release 3.2 was launched by HERMES users in India, and Hermes Release 4.0 was deployed at a first air cargo center in Europe. During the first half of 2009, Hermes expects Release 4.0 to be launched by additional HERMES users in Europe and elsewhere.

In January 2009, we released the Data Replicator for Salesforce.com, a new addition to the iBOLT for Salesforce.com product line.

Vertical Solutions

Two of our subsidiaries develop, market, and support vertical applications, cargo handling solutions and IT professional services.

CoreTech Consulting Group LLC, our wholly-owned subsidiary, is an IT consulting firm offering flexible and creative solutions in the areas of infrastructure design and delivery, application development, technology planning and implementation services, as well as supplemental staffing services.

Hermes Logistics Technologies Ltd., (formerly Magic eCargo), our wholly-owned subsidiary, develops and markets a comprehensive solution for air cargo handling, which is designed to increase productivity, improve efficiency and reduce costs. The Hermes system provides a complete and integrated solution encompassing all physical handling, documentation and messaging requirements, including real-time warehousing, automated build-up of flights/manifesting, messaging to CARGO-IMP standards, customs clearance, weight and balance departure control systems, interfacing, scanning and verification of cargo, secured tracking and a comprehensive financial package for all aspects of billing and collecting fees.

Services

Professional Services. We provide a broad range of consulting and software development project management services to customers developing, deploying and integrating distributed applications. We believe that the availability of effective consulting services is an important factor in achieving widespread market acceptance.

We offer fee-based consulting services in connection with installation assurance, application audits and performance enhancement, application migration and application prototyping and design. Consulting services are aimed at both generating additional revenues and ensuring successful implementation of uniPaaS and iBOLT projects through knowledge transfer. As part of management efforts to focus on license sales, our goal is to provide such activities as a complementary service to our customers and partners.

Services are offered as separately purchased add-on packages or as part of an overall software development and deployment technology framework. Over the last several years, we have built upon our established global presence to form business alliances with our MSPs that use our technology to develop solutions for their customers, and distributors to deliver successful solutions in focused market sectors.

Maintenance. We offer our customers annual maintenance contracts providing for upgrades and new versions of our products for an annual fee.

Technical Support. We believe that a high level of customer support is important to the successful marketing and sale of our products. Our in-house technical support group provides training and post-sale support. We believe that effective technical support during product evaluation as well as after the sale has substantially contributed to product acceptance and customer satisfaction and will continue to do so in the future.

We offer an online support system for the MSPs, which provides them with the ability to instantaneously enter, confirm and track support requests via the Internet. This system supports MSPs and end-users worldwide.

Training. We conduct formal and organized training on our development tools. We develop courses, pertaining to our principal products, uniPaaS and iBOLT and provide trainer and student guidebooks. Course materials are available both in traditional, classroom courses and as web-based training modules, which can be downloaded and studied at the student s own pace and location. The courses and course materials are designed to accelerate the learning process, using an intensive technical curriculum in an atmosphere conducive to productive training

Customers, End-Users and Markets

We market and sell our products and services in more than 50countries worldwide. The following table presents our revenues by revenue type and geographical market for the periods indicated:

	Year ended December 31,		
	2006	2007	2008
	(In thousands)		

	Year ended December 31,		
Software sales	$ 18,788	$ 17,707	$ 20,913
Maintenance and technical support	11,531	12,605	14,530
Consulting services	22,252	28,116	26,537
Total revenues	$ 52,571	$ 58,428	$ 61,980

	Year ended December 31,		
	2006	2007	2008
	(In thousands)		
Israel	$ 4,307	$ 4,471	$ 4,760
Europe	21,713	24,916	25,359
United States	13,995	18,612	20,096
Japan	10,223	9,080	10,110
Other	2,333	1,349	1,655
Total revenues	$ 52,571	$ 58,428	$ 61,980

Industries that are significantly represented by our partners include finance, insurance, government, health care, logistics, manufacturing media, retail and telecommunications. Our uniPaaS and iBOLT technologies are used by a wide variety of developers, integrators and solution providers, which can generally be divided into two sectors: in the first sector are those performing in-house development (corporate IT departments) and in the second sector are MSPs, including large SIs and smaller independent developers, and VARs that use our technology to develop or provide solutions to their customers. MSPs who are packaged software publishers use our technology to write standard packaged software products that are sold to multiple clients, typically within a vertical industry sector or a horizontal business function.

Among the thousands of customers running their business systems with our technology are the following: Access Data, Adecco, Adidas-Canada, Administar Services Group, AFC Worldwide Express, Allstate, Anglo-Canadian Housewares, Anritsu, Athlon Group, Boeing, Burger King, Carey International, City of Phoenix Police Department, Club Med, CBIA, Charlotte Country Court System, Compass Group PLC, Danish Ministry of Economic, Deka Bank, Deutsche Bank, DHL, Electricité de Strasbourg, Electra, Esmee Fairbairn Foundation, Fortis Assurances, Fujitsu-Ten, Euroclear, Europ Assistance Netherlands, Financial Times, FMRP, Fraport AG, GAP, GGD Amsterdam, Grange Insurance, Heller Bank AG, Hitachi, ING Commercial Finance, Johnson & Johnson, John Menzies, Kodak, Lord Corporation, Marconi Mobile, Merrill Lynch, Matsushita, Minolta, NEC, Nestle Nespresso, Nintendo, New York State Public Defenders Association, Online Trading Academy, OTOR, Paris Nord Villepinte Exhibition Center, Philip Morris, Primagas, Prestwick House, Rosenbauer, San Francisco Courts, Semeru, Sharp System Products, Sklar Peppler, TEVA, Title Solutions, Titan Software, Vadim Software, Vodafone, the United Nations, UPS, Victorinox, Vodafone, W3Com, Warren Board and Washington State.

Sales, Marketing and Distribution

We market, sell and support our products through our own direct sales force as well as through a global channel-network of ISVs, SIs, value-added distributors and resellers, as well as OEM and consulting partners. Our own sales force is based in our regional offices in the United States, Japan, the United Kingdom, France, Germany, the Netherlands, Hungary, India and Israel, and through local distributors elsewhere, our channel-network is present in about 50 countries worldwide.

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