



CONNECT INNOVATION REPORT

A QUARTERLY EVALUATION OF OUR INNOVATION ECONOMY IN SAN DIEGO AND ACROSS CALIFORNIA

Q3.09

New Start-ups / VC Investment / M&A Activity / New Patents / Research Grants / Research Employment

NEW START-UPS SLOW, FEDERAL GRANT FUNDING IN SAN DIEGO JUMPS IN THIRD QUARTER 2009

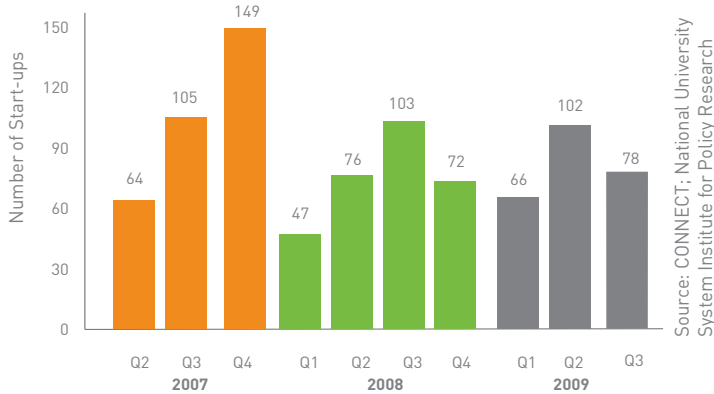
The pace of new technology start-ups in San Diego slowed in the third quarter of 2009, but federal grant funding from the National Institutes of Health was up 44% and National Science Foundation grants doubled, CONNECT's newly released Third Quarter 2009 Innovation Report shows. Start-ups were down 24% with 78 companies launched in the third quarter compared to 102 companies in the second quarter of 2009.

The CONNECT Innovation Report (CIR) is the first to provide an economic indicator of the strength and impact of the innovation economy in San Diego. Published each quarter by CONNECT, San Diego's technology and life sciences accelerator, the Report includes:

- New innovation start-ups
- Venture capital investment
- Mergers and acquisition activity
- New patent applications and patents granted
- Research grants
- Research employment and wages

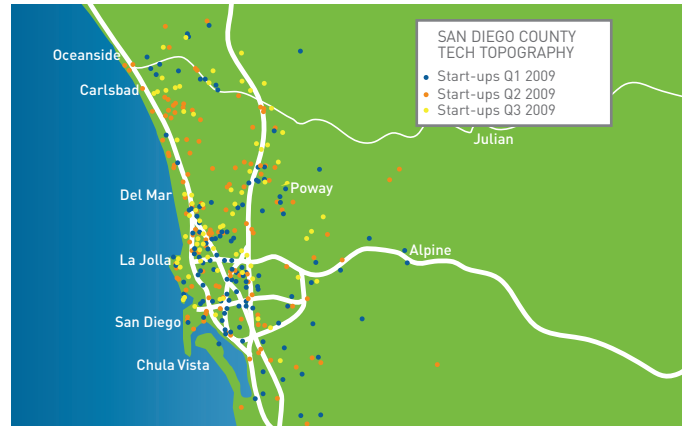
Statewide, San Diego accounted for 13% of new technology businesses in the third quarter of 2009 ranking third after Los Angeles (LA) and Santa Clara counties. LA had 105 start-ups, down from 140 in the previous quarter, and Santa Clara had 100, down from 117 new companies.

SAN DIEGO INNOVATION START-UPS BY QUARTER



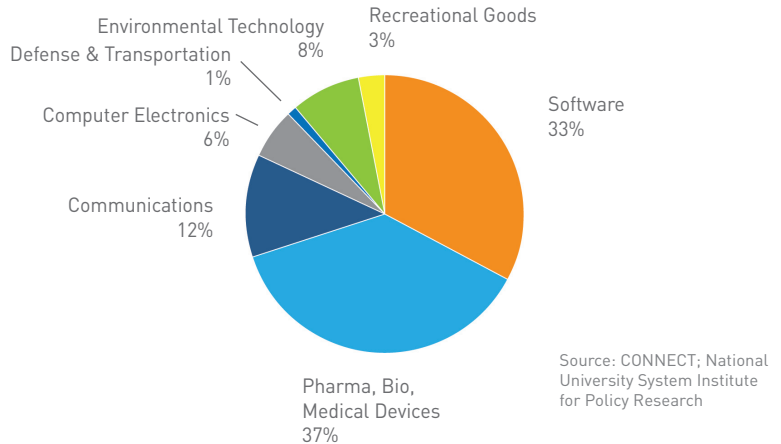
San Diego continued to have the most life science start-ups of any county across the state in the third quarter. This was down 22% from the 37 companies formed in the second quarter. San Diego's software sector showed the strongest gain in number of new companies with 26 new companies – up 18% from 22 start-ups in the second quarter of 2009. The communications sector ranked third with 9 start-ups. California showed a similar slowing in start-up creation in the third quarter with 617 new technology companies established compared to 729 in the second quarter – a 15% decrease. This was also down 15% from the third quarter of 2008 when 730 companies were started.

Mirroring the trend in San Diego, the software sector accounted for the highest number of technology start-ups in the third quarter of 2009 with 192 new companies statewide. Pharma/biotech/medical devices followed with 138 start-ups. The communications sector was the only industry showing an increase in start-ups over second quarter figures with 103 new companies, up 14% over the 90 companies established in the previous quarter. The largest decrease in new company formation was in the recreational goods (action & sports) sector



with six start-ups in the third quarter, down 60% from 15 in the second quarter. Year-on-year, start-ups in the defense & transportation (24) were up 20% and environmental (cleantech) technology (48) sectors were up 14%.

SAN DIEGO START-UPS BY INDUSTRY - THIRD QUARTER 2009



EARLY STAGE COMPANIES ATTRACT ALMOST 70% OF SAN DIEGO VC FUNDING

Venture capital investment in San Diego was up 18% from the third quarter of 2008 with 32 local companies receiving \$236 million, according to the latest PricewaterhouseCoopers/National Venture Capital Association MoneyTree™ quarterly report.

The amount of VC funding was down slightly (6%) from the \$252 million raised by 28 San Diego companies in the second quarter of 2009. Both the second and third quarter figures were up significantly – over 150%, from the \$92 million raised by 15 companies in the first quarter of this year. The biotechnology, medical devices and healthcare services sector received the majority of the financing during the third quarter, with \$155 million, or 66%, of the total funds invested in San Diego. This is down slightly from \$159 million invested in the life science sector in the second quarter of 2009, and up over the \$24 million invested in the third quarter of 2008.

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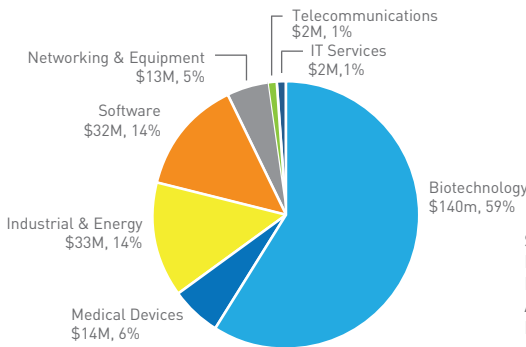
SUMMARY OF NATIONAL & REGIONAL VC INVESTMENTS

Region		2007	2008	2009 Q1	2009 Q2	2009 Q3
United States	Total (in Billions)	\$30.9	\$28.3	\$3.2	\$4.1	\$4.8
	# of Deals	3,952	3,808	603	657	637
	Average (in Millions)	\$7.8	\$7.4	\$5.3	\$6.3	\$7.5
California	Total (in Billions)	\$14.7	\$14.3	\$1.5	\$1.8	\$2.7
	# of Deals	1,626	1,552	229	259	277
	Average (in Millions)	\$9.0	\$9.2	\$6.4	\$7.0	\$9.8
Northern CA*	Total (in Billions)	\$11.1	\$11.1	\$1.3	\$1.4	\$2.2
	# of Deals	1,255	1,189	187	195	212
	Average (in Millions)	\$8.9	\$9.3	\$6.9	\$7.1	\$10.5
Southern CA**	Total (in Billions)	\$3.6	\$3.2	\$0.3	\$0.4	\$0.5
	# of Deals	371	363	55	64	65
	Average (in Millions)	\$9.7	\$8.8	\$5.5	\$6.7	\$7.3
San Diego	Total (in Billions)	\$2.0	\$1.2	\$0.09	\$0.25	\$0.24
	# of Deals	163	126	15	28	32
	Average (in Millions)	\$12.0	\$9.7	\$6.0	\$9.0	\$7.4

* Includes Silicon Valley and Sacramento County, Orange County and San Diego County.
 ** Includes Los Angeles Association MoneyTree™ Report; CONNECT

San Diego led the nation in the proportion of total VC financing of start-up and early stage companies. San Diego experienced an 11% increase in the amount of funding going to start-up/early stage companies in the third quarter of 2009. In total, 67%, or nearly \$160 million of total investment went to these stage companies. Financing of later stage companies fell to 14% of the total in San Diego compared to 37% in the second quarter of 2009. Silicon Valley and New England shared the top spots in the amount of VC investment in seed/early stage companies. Silicon Valley start-ups attracted nearly \$590 million and New England start-ups garnered \$267 million. Vanessa Herbert, Senior Manager at PricewaterhouseCoopers, noted, "...a majority of the investments are seed and early stage funding...Even with the small opening in the initial public offering window, venture capitalists appear to continue focusing their San Diego investments towards initial stage companies."

SAN DIEGO VC INVESTMENTS BY INDUSTRY - Q3 2009



Source: PricewaterhouseCoopers/National Venture Capital Association MoneyTree™ Report; CONNECT

MERGERS AND ACQUISITIONS DEALS INCREASE

Mergers and acquisition deal activity increased in the third quarter of 2009 compared to the previous quarter in San Diego and the rest of the state, though total reported transaction values were lower. In San Diego, 32 deals were closed in the third quarter compared to 24 in the second quarter. The number of deals reported closed in southern California increased to 134 and in northern California to 155 deals in the third quarter of 2009.

Regional M&A Activity

Region		2009 Q1	2009 Q2	2009 Q3
Northern CA	Total Reported Value (in Millions)	\$4,949	\$1,866	\$2,520
	# of Closed Deals	91	89	155
Southern CA	Total Reported Value (in Millions)	\$6,195	\$1,169	\$1,827
	# of Closed Deals	103	74	134
San Diego	Total Reported Value (in Millions)	\$2,703	\$139	\$99
	# of Closed Deals	42	24	32

Source: IQ Capital; ROTH Capital Partners

Selected Reported Q3 2009 San Diego M&A Deals

Packet Video acquired by NTTDoCoMo, Inc.	\$45.5M
AnySourceMedia, LLC acquired by DivX, Inc.	\$15.0M
PostHypothermia Corp. acquired by Philips Electronics N.A.	\$11.3M

PATENTS GRANTED UP ACROSS THE STATE

In San Diego, 791 patents were granted in the third quarter of 2009 - up over 14% compared to the previous quarter when 691 patents were granted. San Diego accounted for 17% of the patents filed in California in the third quarter, and 12% of the patents granted. Patent applications were down slightly (7%) in the third quarter with 1,445 applications filed compared to 1,559 in the second quarter of 2009.

Similar results were found regionally across the rest of the state. The number of patents granted was up in all three regions in the third quarter while applications were down, the largest decrease being in northern California where patent filings falls 24% to 4,829 from 6,320 in the second quarter of 2009.

NEW PATENT ACTIVITY IN KEY INNOVATION CENTERS

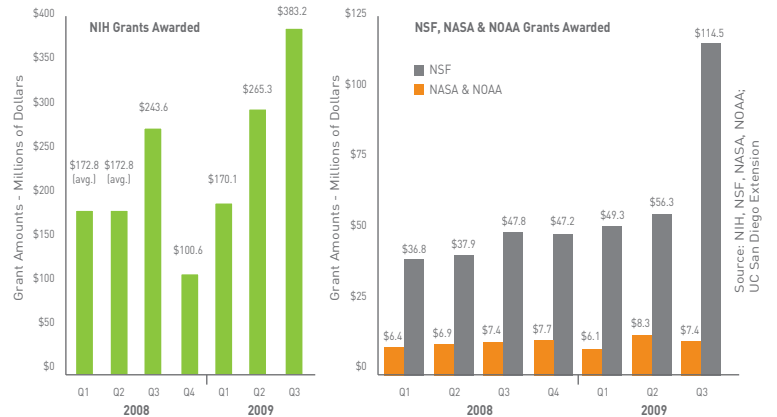


Source: University of California, San Diego Extension, USPTO

NIH AND NSF FUNDING JUMP TO NEW HIGHS

Federal grant funding exceeded VC investment in San Diego in the third quarter. Federal research grants awarded in San Diego were up significantly in the third quarter of 2009. Grant funding awarded by the National Institutes of Health (NIH) increased 44% to over \$383 million compared to \$265 million in the second quarter of 2009. National Science Foundation (NSF) reported \$115 million in grants awarded in San Diego in the third quarter of 2009 - double the amount awarded in the previous quarter. Research grants from the National Aeronautics and Space Administration (NASA) totaled over \$3 million and the National Oceanic and Atmospheric Administration (NOAA) reported just over \$4 million in awards.

FEDERAL RESEARCH GRANTS RECEIVED FOR SAN DIEGO



Source: NIH, NSF, NASA, NOAA; UC San Diego Extension

RESEARCH WAGES AND JOBS DOWN SLIGHTLY

This section of our report compares the latest available data on employment and average weekly wages paid by private research institutions across several regions. In San Diego, both wages and employment fell slightly in the first quarter of 2009. Average weekly wages in San Diego were similar to those reported across the southern California region, but lagged behind those in northern California and Boston. Northern California had nearly 57,000 employees in the first quarter compared to 52,000 in the southern California region.

REGIONAL PRIVATE RESEARCH INSTITUTES WAGES & EMPLOYMENT



Source: Quarterly Census of Employment, US Bureau of Labor Statistics