STARTUP OUTLOOK
2010

SVB Financial Group

Silicon Valley Leadership Group

Message from SVB Financial Group

Coming off of one of the most difficult years in memory for small businesses, conditions for startup technology companies are showing signs of modest improvement.

As a partner to technology companies for nearly 30 years in Silicon Valley, across the U.S. and increasingly throughout the world, we have had the privilege of watching entrepreneurs lead the way out of down economic cycles time and again. Without a doubt, many challenges remain. But our clients are telling us that things are looking up.

The results of our first Startup Outlook Survey, which complements the Silicon Valley Leadership Group's Annual CEO Business Climate Survey, confirmed many of our experiences of late with young, dynamic technology and life science companies in the United States. On balance, they are optimistic and expect to grow and create jobs this year.

Specifically, most surveyed companies expect their 12 month performance outlook to improve, and nearly three quarters expect to hire new employees in 2010. However, many continue to cite access to capital as their number one challenge to growth. As corporations, institutions and consumers begin to loosen their purse strings and start to invest in new products and services that will make them more efficient, secure, connected, cleaner or healthier, small technology and life science businesses will have more opportunities to generate sales and subsequently growth capital and financing.

The role of government also plays an important role in a startup company's ability to succeed, as suggested by the survey results. More than half of our survey respondents cited government funding and R&D grants as the top priority for government focus in order to create jobs and financial growth in the business sector.

Like the Silicon Valley Leadership Group, we are dedicated to understanding the environment in which our clients and constituents operate, identifying and sharing the tools they need to succeed and doing our best to increase their probability of success.

We look forward to your reaction to our clients' perspectives and outlook, in addition to a productive year of growth and innovation.

Sincerely,

Ken Wilcox
President and CEO
SVB Financial Group

Carl Guardino
President and CEO
Silicon Valley Leadership Group

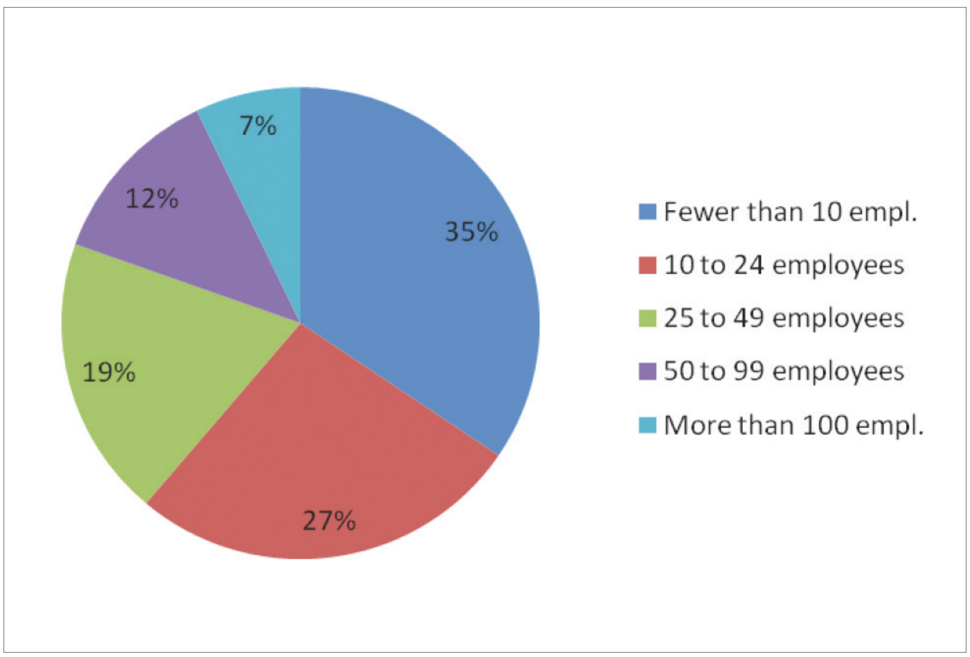
Executive Summary

About the Survey and the Participants

SVB Financial Group's Startup Outlook 2010 survey sheds light on the business environment as experienced by U.S.-based startup technology and life science companies. As one of few institutions dedicated to the innovation sector, SVB works with interesting, creative entrepreneurs who have the potential – literally – to disrupt, improve and change the world. As we continue to find ways to help them succeed, we have asked them to describe their perception of the business environment in 2010, their greatest challenges, and the areas in which government can help support their growth.

Capturing the sentiment of startup companies nationwide, our online survey conducted in February 2010 generated 304 responses by U.S.-based emerging and early-stage technology and life science companies with annual revenues less than $5 million. The majority of responding companies (81 percent) employ fewer than 50 employees. Throughout this report, the results were consistent for all U.S. regions, but where significant differences occurred, results are broken down by California versus non California companies. Of note, 76 percent of the 127 respondents from California were from the San Francisco Bay Area, offering specific insights into perceptions among startups in Silicon Valley in particular.

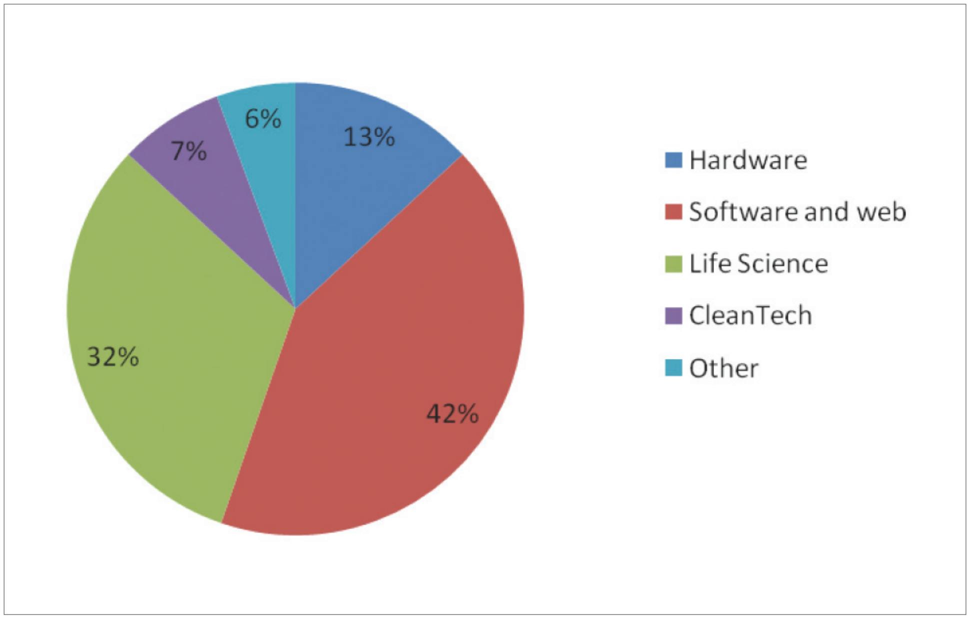
Company Size



Executive Summary *(continued)*

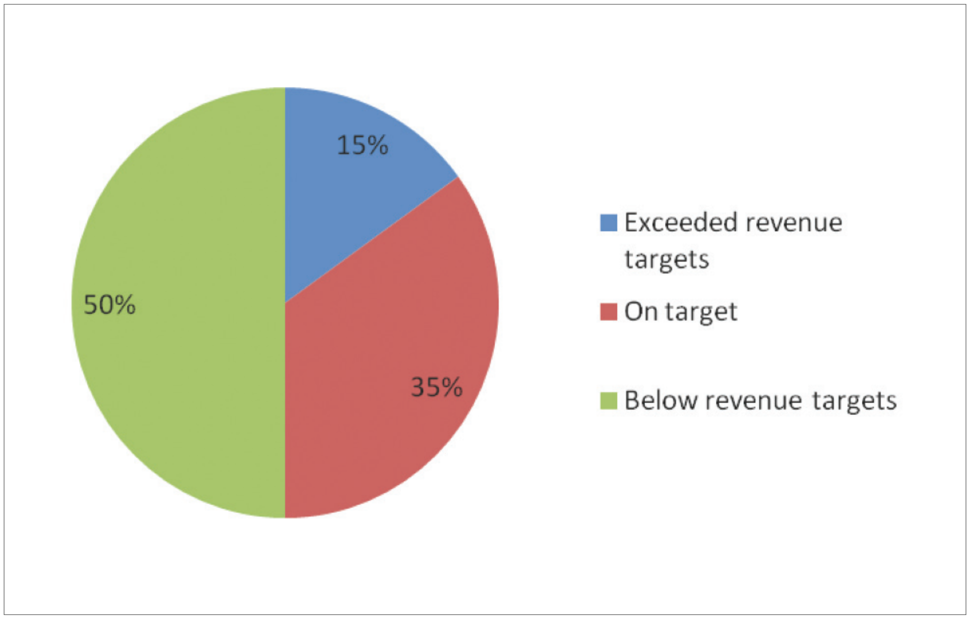
The respondents represented a cross-section of the technology sector.

Industry Niche



Not surprisingly, respondents confirmed that 2009 was a tough year, with fully half missing expected revenue targets.

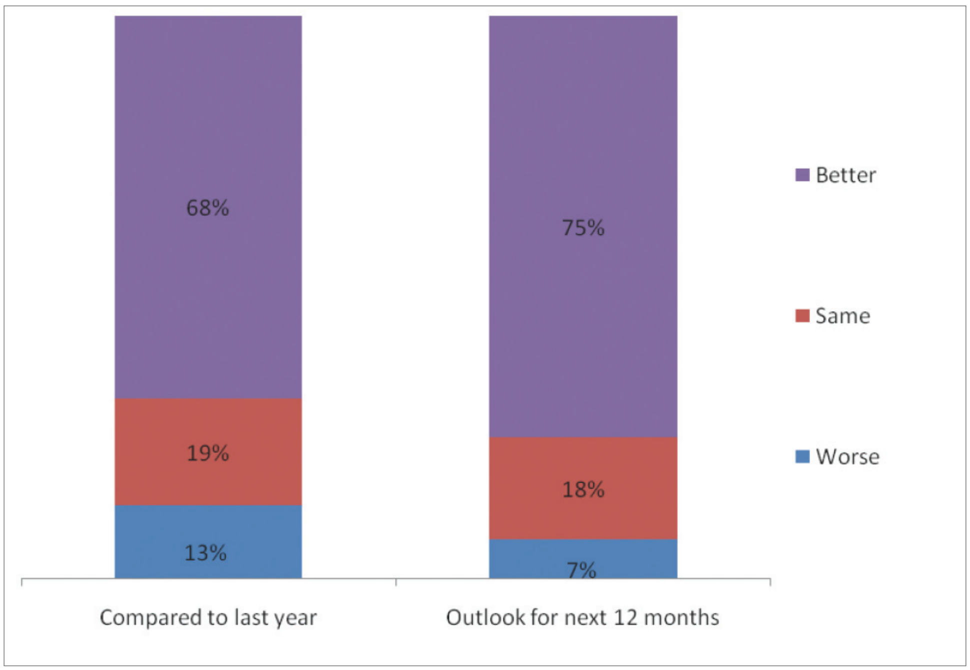
2009 Company Performance



Executive Summary *(continued)*

The majority, however, did report (65 percent in California versus 75 percent elsewhere in the country) that they expected to see improvements in 2010, particularly in the hardware and software sectors. Some cited an increase in sales and quicker decision-making among their customers or expansion into new lines of business as the sources for their optimistic view. While more than half of life science companies expected better business conditions in the coming year, they were markedly less optimistic than the other technology sectors.

Business Conditions for Startups



Hiring, reduced competition, access to capital, customer acquisition and retention and the need for government support in R&D funding rose to the top as some of the greatest opportunities, challenges and needs of startup technology companies.

Throughout the report, we've noted potential explanations for certain responses as well as insights offered by some of SVB Financial Group's sector experts. With most questions, respondents were given the opportunity to add observations and comments, which are included throughout the report to provide more in-depth perspectives in the executives' own words.

We would like to thank our partner Koski Research for helping to develop and conduct the survey, as well as SVB's industry experts, bankers and researchers for their analysis and perspectives on the data.

Key Findings

- The vast majority – 74 percent – of emerging technology and life science companies are planning to hire new employees in 2010
- In the face of extremely high unemployment levels, it's notable that nearly a quarter of all companies listed access to talent as a challenge, perhaps implying a pending talent war
- Among the challenges facing startups, access to capital was listed as the number one concern
- Companies believe reduced competition due to the economic climate will create opportunities for those still in business
- Respondents believe that the primary ways the federal government can help startup companies is with a focus on R&D grants, healthcare reform, tax policies and intellectual property protection

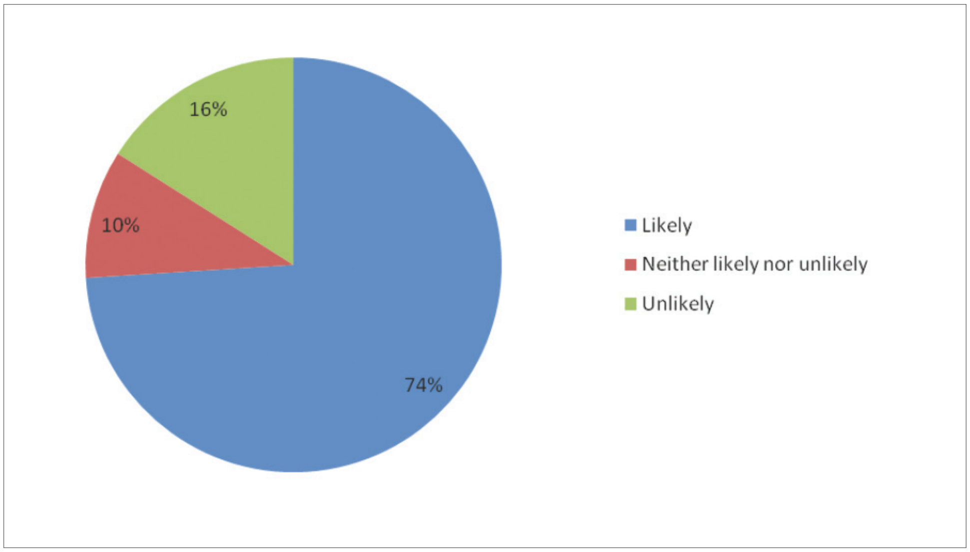
Creating Jobs

Emerging companies contribute significantly to job creation in the U.S. The National Venture Capital Association reported there were 12.1 million jobs at venture capital-backed companies in the United States in 2009, and those firms accounted for 21 percent of U.S. GDP. Today, there are more than 12,000 jobs available at venture capital-backed companies listed on StartUpHire.com, up from 11,000 posted jobs just four months ago. At a time when the national unemployment rate is topping 10 percent, the outlook provided by emerging companies in this survey is also hopeful, with three-quarters expecting to hire new employees in the next 12 months.

Of the companies that are planning to hire, 86 percent will create jobs within the state where they are headquartered, 30 percent will hire in another U.S. state and 21 percent are planning to hire employees abroad.

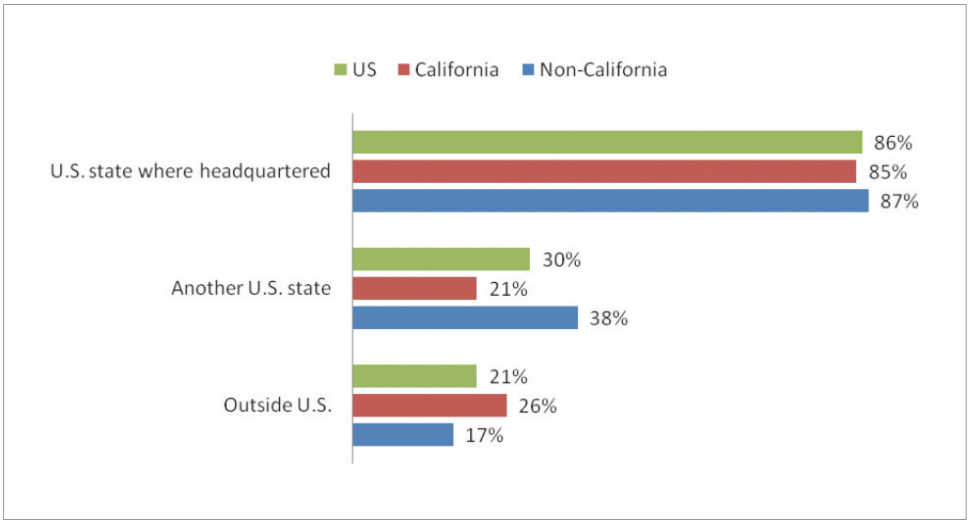
California companies are less likely to hire employees in another U.S. state but are more likely than the national average to hire employees abroad.

Likelihood to hire new employees in the next 12 months



Creating Jobs *(continued)*

Location where likely to hire (not mutually exclusive)



Keeping Startups Awake at Night

The top three most challenging issues facing technology and life science startup companies, according to survey respondents, were access to capital, general business conditions and the regulatory climate. Intellectual property rights and protections, managing expenses and access to talent followed in priority order.

Access to Capital

The steep decline in venture capital investment in 2009, the lack of exit opportunities for startup companies to go public or get acquired and tightening loan requirements of many banks are consistent with the respondents' perception that it is difficult to obtain capital in the current environment. It stands to reason that emerging companies need capital investments to grow; however, more investment does not necessarily drive demand for a product or service. Access to capital likely references a company's ability to raise equity. Venture investment was off by 37 percent in dollars in 2009 over 2008, but it's not venture investment alone that has declined. Until the public markets re-open, companies will continue to struggle to find capital at the early and later stages.

Silicon Valley Bank's experience during 2009 echoes the executives' responses only in part. During 2009, Silicon Valley Bank remained active in the market, adding 400 new borrowers and continuing to lend. At the same time, we saw many companies choose to deleverage (or, in other words, to pay down existing loans and minimize new borrowings to the extent possible). Once companies begin to see their sales pick up, SVB anticipates that businesses will once again increase their borrowings in order to fund inventory, equipment, space, employees, and other assets, and lenders other than SVB (that reduced their level of activity during the downturn) will become more active once again.

Thus far in 2010, there has been a slight improvement in the number of companies registered to go public, the merger/acquisition appetite of larger corporations, the need of institutions to make capital improvements and technology investments, and the investment appetite of venture capital investors. All of these factors may help startups begin to feel that they have access to the financing they need to continue to grow.

Keeping Startups Awake at Night *(continued)*

General Business Conditions

As business conditions slowly improve, and customers begin to spend, the innovation sector likely will be one of the early beneficiaries. The efficiencies, security, productivity gains, avoiding obsolescence, and other benefits that most technology companies offer create a compelling value proposition, encouraging customers to continue to make investments even during difficult times. In their open-ended responses, the executives we surveyed cited acquiring customers and getting them to make faster purchasing decisions as one of their biggest challenges in today's environment.

> *"We are a B to B company with a focus on small to medium businesses. If the economy remains tough, we could lose some customers because they can't afford our product."*

Despite the many challenges facing emerging technology and life science companies, many also found opportunities in such a dismal economy. Namely with less competition, some stated their chances of success improved. In their own words, a few sounded optimistic for their prospects:

> *"Because of the recession, we have a more level playing field against the gazillion dollar marketing budgets. This is because companies are FORCED to actually look at what they are buying."*

> *"A drastic reduction in the amount/number of qualified, sustainable competitors in our technology sector will yield opportunity in the future."*

> *"Competition is lessened due to recessionary attrition. We are surrounded by opportunities."*

Involving the Government

Consistent with the central role the federal government plays in funding research and early stage companies' ever-present need for growth capital, more than half of the respondents ranked federal government R&D funding and grants as the top priority to help young companies innovate and grow, particularly among life science companies.

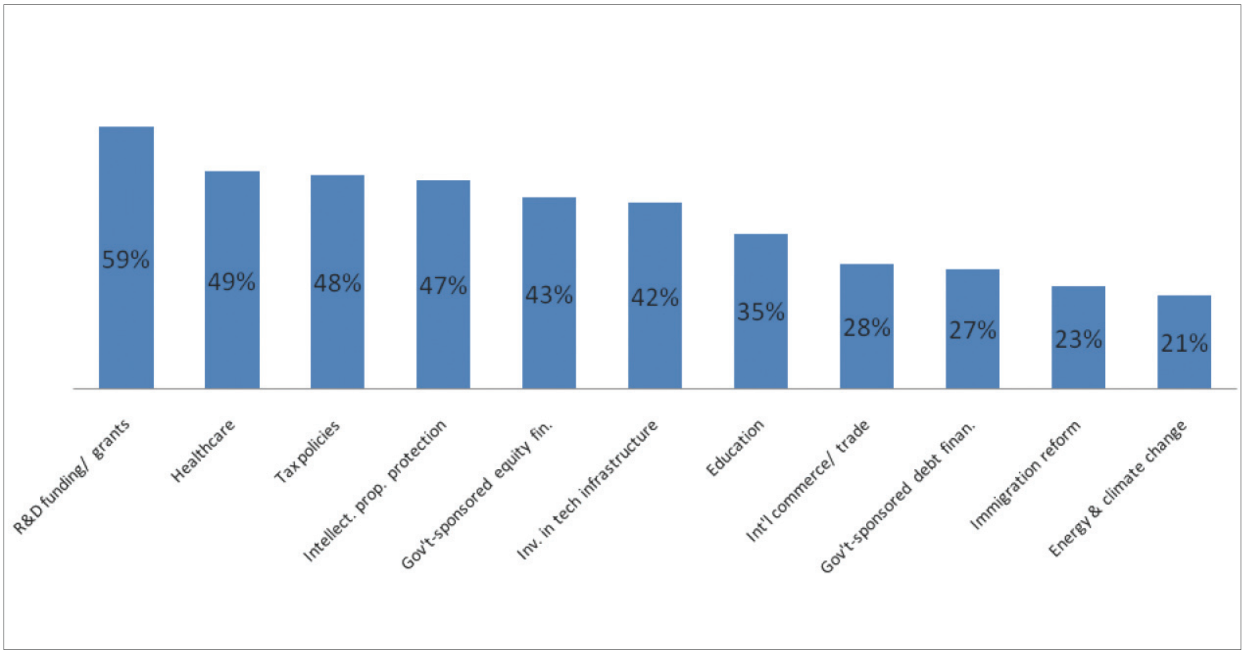
Respondents also cited healthcare as an important priority for the federal government by startups, although respondents were somewhat split on the direction of proposed reforms. (We conducted our survey before the healthcare reform bill was passed in March 2010.) While some startups saw healthcare reform as a way to better compete with larger organizations, others worried about the effect reform would have on their business in terms of costs and innovation. Historically, healthcare has been a large financial burden for startup companies, where the corporate economies of scale do not exist for small numbers of employees. Not surprisingly, life science companies are more interested in this area (61 percent versus 42 percent of other technology companies identified this as a key priority) and expressed their desire for a prompt resolution of the healthcare debate in order to have clear rules going forward.

Tax policies and intellectual property protection were also seen as key areas for government focus. Direct government investment in technology companies, or in the form of technology infrastructure spending, was seen as a priority by about 40 percent of the respondents.

Key Findings

Involving the Government *(continued)*

Where should the government focus to create growth



Many respondents had specific suggestions for the role of the federal government when asked how it may help an emerging technology or life science company grow, compete and succeed:

> *"The opportunity is in accelerated research funding and the government must lead […]. Patent reform would be nice, it doesn't favor small companies."*

> *"Government investment in cyber-security, commercial interest in fraud detection / loss minimization and business intelligence given the enormous amount of information that is being created, transferred and stored with every economic event."*

> *"Smart Energy regulations, support and deployments - Smart Grid, Smart Meters, and Smart Homes. This is largely a state government issue (PUC). Deregulation of the energy market would be very helpful to enable innovation in energy, however this is highly unlikely."*

> *"Healthcare policy clarity and a stabilizing, predictable approach from FDA can return interest to the medical technology and healthcare spaces."*

> *"Government [should] focus on small business revitalization and on technology/sciences education drive."*

> *"Government spending is out of control and unsustainable. Taxes at both Federal and CA State level are utterly ridiculous and grounding our business. Both the Fed and CA state governments have become the enemies of capitalism in America."*

Sector Findings

Comparing the responses between technology sectors brought to light a number of additional key findings of interest.

Hardware – Access to Talent

In the face of extremely high unemployment levels, it's notable that nearly a quarter of all companies listed access to talent as a challenge, perhaps implying an upcoming war for talent. Breaking that down further, it is clearly the hardware sector (29 percent) that appears to have the greatest issue with finding qualified candidates (versus life sciences at 15 percent). Interestingly, hardware companies also have the highest percentage of companies listing immigration reform as a critical focus area for the government (32 percent), compared, for example, to life science respondents (13 percent). In addition, more hardware companies list education as an issue (40 percent) than life science companies (29 percent). This suggests that the U.S. is not graduating enough electrical engineering students so access to overseas talent has become much more important in the hardware sector, and may explain why education ranks the highest issue for government support. Additionally, it typically takes more time and experience to develop a seasoned engineer working in the semiconductor industry, which may also contribute to the need for more education in the hardware sector, as opposed to the software sector, for example.

Life Sciences – A Tougher Startup Environment

Noticeably and predictably, there are distinct differences between the responses from the life science sector and other technology sectors in terms of their outlook, challenges and areas of proposed government focus.

Overall, life science companies had a less optimistic view of the next 12 months with 55 percent indicating business conditions would be better in the coming year, as opposed to 81 percent of software companies and 86 percent of hardware companies anticipating better business conditions in the year ahead.

Clearly the regulatory climate, which is known to be difficult in the U.S., is an enormous issue for life science companies with 70 percent citing it as an important area for government focus. Only 27 percent of hardware and 29 percent of software companies listed the regulatory climate as a priority. Companies and life science venture capital investors anecdotally concur that the FDA is extremely slow and increasingly conservative.

R&D funding, healthcare and IP were highly ranked by life science companies, significantly higher than hardware and software company rankings, in terms of the areas of government focus required for their growth. Access to capital was the biggest challenge listed for all sectors, but for life sciences it was critical for 74 percent of respondents, versus 67 percent for software and 60 percent for hardware.

Only 31 percent of life science companies reported missing 2009 revenue targets, as opposed to nearly half of hardware companies and 60 percent of software companies. Nevertheless, the life science sector reports it is in a tougher position currently than the other startups surveyed.

Cleantech – Tied to Policy and Investment

Given the emergent nature of the cleantech industry, we received a smaller number of responses from executives in this sector. While this prevents us from drawing statistically meaningful conclusions about cleantech, directionally it provides some interesting insights.

Like their peers elsewhere in the technology sector, cleantech executives expect to hire in the next 12 months (almost 90 percent), typically will hire in the state in which they are headquartered (over 80 percent), and see their top challenges as access to capital and general business conditions.

Their views on policy matters, however, diverge from their peers. They rank R&D funding, energy/climate legislation, investment in infrastructure, and government-sponsored debt financing as the top priorities.

Sector Findings *(continued)*

These views are not surprising. Across the board, the cleantech sector is seen as uniquely intertwined with government policy. Yet these views do provide further evidence for some important conclusions. One, cleantech companies have the potential for meaningful job creation. Two, government investments in R&D and energy infrastructure will help lay the foundation for the sector's long-term success and for U.S. leadership in this expanding industry. Three, the need for meaningful new climate and energy policies should not be seen solely through the lens of climate change, but should be recognized as an issue affecting U.S. competitiveness and economic development. And, four, that agencies such as the Department of Energy and the Export-Import Bank should take steps to ensure loan guarantee and other lending programs reach small, innovative companies.

Next Steps

Armed with the observations and needs of the startup sector we exist to support, SVB Financial Group will be taking these findings on the road to share the needs of revenue, job and innovation-creating entrepreneurs and companies with our legislators. As a company built solely to help entrepreneurs succeed, we feel it is incumbent upon us to recognize and address the needs of our clients.

The venture-backed segment of our economy stimulates significant revenue, jobs and competitive advantages for America. It is in all of our best interests to maintain focus on creating an environment in which emerging technology and life science companies can compete fairly and access capital, talent, and legislative and regulatory support they need to grow, and therefore contribute to a healthy and vibrant U.S. economy.

With dedicated experts focused on sectors including software, cleantech, hardware and life sciences, we are committed to representing and raising the voice of entrepreneurs and their investors with all constituencies we believe can help them prosper.

About SVB Financial Group

For nearly 30 years, SVB Financial Group and its subsidiaries, including Silicon Valley Bank, have been dedicated to helping entrepreneurs succeed. SVB Financial Group is a financial holding company that serves companies in the technology, life science, venture capital/private equity and premium wine industries. Offering diversified financial services through Silicon Valley Bank, SVB Analytics, SVB Capital, SVB Global and SVB Private Client Services, SVB Financial Group provides clients with commercial, investment, international and private banking services. The company also offers funds management, broker-dealer transactions and asset management, as well as the added value of its knowledge and networks worldwide. Headquartered in Santa Clara, Calif., SVB Financial Group (Nasdaq: SIVB) operates through 27 offices in the U.S. and international operations in China, India, Israel and the United Kingdom. More information on the company can be found at www.svb.com.

Silicon Valley Bank is the California bank subsidiary and the commercial banking operation of SVB Financial Group. Banking services are provided by Silicon Valley Bank, a member of the FDIC and the Federal Reserve System. SVB Financial Group is also a member of the Federal Reserve System.

Notes

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