

ACCOUNTABILITY REPORT 2012-2013

innovacorp

EARLY STAGE VENTURE CAPITAL

We get invested.

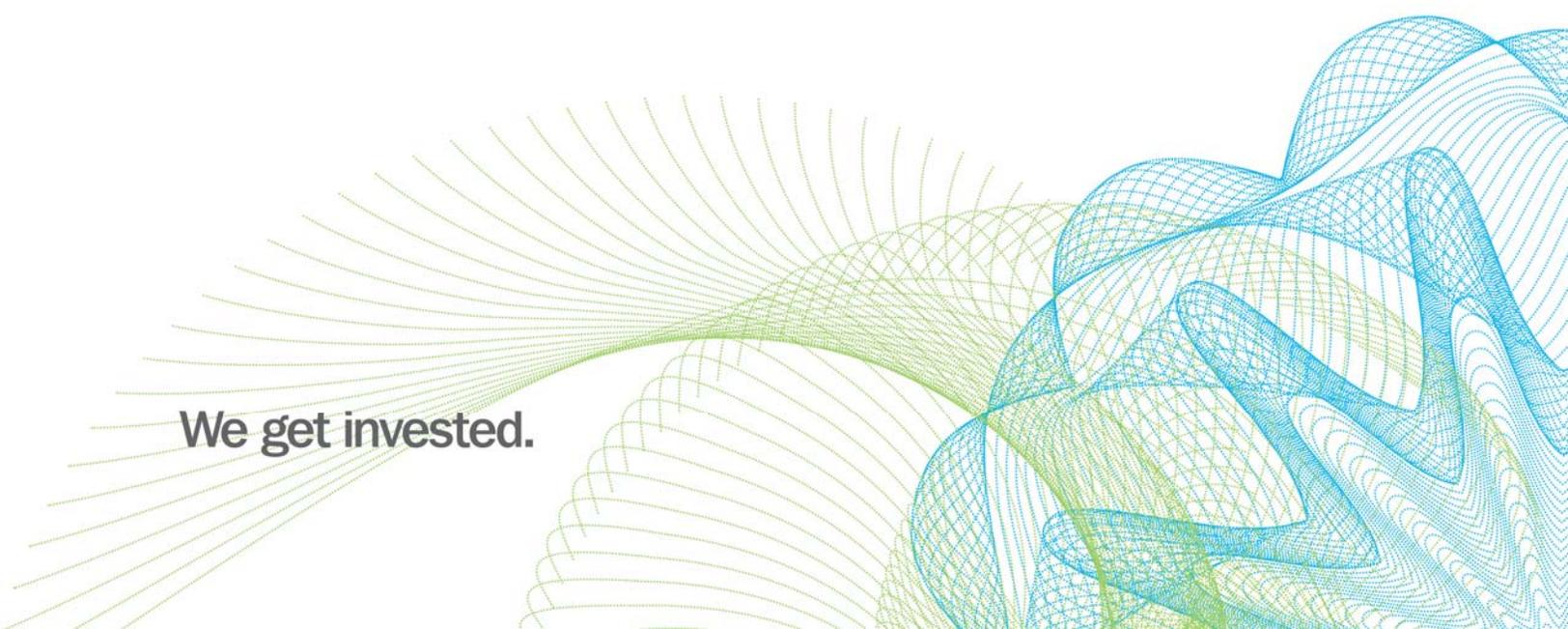


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Accountability Statement

Innovacorp's accountability report for the year ended March 31, 2013, is prepared pursuant to the Finance Act and government policies and guidelines. These authorities require the reporting of outcomes against Innovacorp's business plan for the fiscal year 2012-2013. The reporting of Innovacorp's outcomes necessarily includes estimates, judgments and opinions by Innovacorp management.

We acknowledge that this accountability report is the responsibility of Innovacorp management. The report is, to the extent possible, a complete and accurate representation of outcomes relative to the goals and priorities set out in Innovacorp's business plan for the year.

Honourable Graham Steele
Minister, Economic and Rural Development
and Tourism

Jacquelyn Thayer Scott
Chair, Innovacorp Board of Directors

Stephen Duff
President & CEO, Innovacorp

Introduction

This accountability report covers the Innovacorp business plan for 2012-2013 and therefore should be read in conjunction with that plan, which you can download at www.innovacorp.ca/about-us/corporate-publications. The report reviews the goals and priorities set in the spring of 2012 and describes the accomplishments and progress achieved during the period ending on March 31, 2013. Financial results are provided with an explanation for any significant budget variances.

As Nova Scotia's early-stage venture capital organization, Innovacorp plays an important part in the province's *jobsHere* economic plan. The young, knowledge-based companies Innovacorp invests in and assists are innovative and globally competitive, and they create good jobs. These start-ups are vital to growing our economy.

Capital is the lifeblood of any early-stage company. The emerging companies in Innovacorp's portfolio require risk capital to help fund their start-up and early development phases. Nova Scotia is considered an underserved market when it comes to access to risk capital, so the Province of Nova Scotia, through Innovacorp, plays an important part in supporting these promising companies.

In 2012-2013, Innovacorp continued to focus on enhancing our pipeline of investment opportunities, making investments in high-potential companies, and working closely with these companies to help them achieve success. We also worked with our private and public sector regional venture fund partners to successfully launch this important new source of capital.

Last year, our portfolio companies generated about \$22.1 million in export revenue and directly employed about 312 people, resulting in a payroll of about \$22.8 million, most of which was in the form of high-value jobs. Furthermore, the investments we made in 2012-2013 leveraged an additional \$6.19 million in investment from other sources.

Along with venture capital investment, Innovacorp provided tailored, hands-on business guidance to the companies it invested in. It also delivered world-class incubation services and facilities – places Nova Scotia's technology entrepreneurs can call home. At fiscal year end, Innovacorp's incubation facilities, including the Technology Innovation Centre (TIC) in Dartmouth and the Innovacorp Enterprise Centre (IEC) in Halifax, stood at 97 per cent occupancy.

The following pages provide details about Innovacorp's activities and accomplishments in 2012-2013. We are proud of our results, but there is always more that needs to be done. We look forward to 2013-2014 and further increasing innovation, entrepreneurship, and the number of business success stories in Nova Scotia.

Innovacorp Progress and Accomplishments 2012-2013

As Nova Scotia's early-stage venture capital organization, Innovacorp is an important part of the province's start-up ecosystem. The young, knowledge-based companies that we invest in and assist are innovative and globally competitive and are vital to growing our economy. Our business model incorporates seed and early-stage venture capital, hands-on business guidance, and world-class incubation facilities, to help entrepreneurs overcome traditional hurdles to business growth.

As stated in our 2012-2013 business plan, our performance for that year can be measured against two goals and four priorities.

Goal 1: *To fuel sustainable economic growth by enabling Nova Scotia knowledge-based companies to accelerate the commercialization of their technologies and increase competitiveness in export markets.*

Nova Scotia's ability to compete – regionally and globally – is increasingly reliant on the success of its knowledge-based companies. These high-growth ventures positively affect the province's prosperity.

Goal 2: *To collaborate with private and public partners to build a dynamic high-growth entrepreneurial culture in Nova Scotia.*

Innovacorp continually collaborates with entrepreneurs, private sector organizations, professional services firms (e.g., legal, accounting), angel and venture capital investors, academia, industry associations and public sector agencies to help create a dynamic entrepreneurial culture throughout Nova Scotia and deliver on the province's *jobsHere* strategy to grow the economy.

Priorities

1. Maximize the Impact of the Nova Scotia First Fund

Innovacorp is Nova Scotia's early-stage venture capital organization. One of Innovacorp's key assets is the Nova Scotia First Fund (NSFF). The fund targets emerging venture-grade technology companies with high-growth potential and attractive risk-return prospects. Innovacorp's strategy has been to strengthen the goodwill and credibility for the region and to build the return track record of the asset class, thereby attracting more capital to the region. A priority in 2012-2013 was to maintain our investment pace by making 7-10 investments in early-stage Nova Scotia companies in the information technology, life sciences and clean technology sectors.

- In 2012-2013, Innovacorp invested \$5.18 million in 12 promising technology companies in Nova Scotia, and these investments leveraged an additional \$6.19 million in investment from other sources. While maintaining high-quality due diligence and staying on budget, the deal flow stayed at the previous year's record level.
- In July 2012, Golnstant, a Halifax-based developer of a shared web-browsing solution, was purchased by U.S.-based Salesforce.com. In 2011, Innovacorp invested \$100,000 in Golnstant, alongside investors such as Freestyle Capital; Baseline Ventures; Greylock Partners; Social Leverage; Yuri Milner; and Reid Hoffman. Innovacorp realized a 10-fold return on investment for this exit.

- Along with our financial investment comes hands-on guidance for portfolio companies, helping them reach milestones towards commercial success. For example, with assistance from Innovacorp, portfolio company aioTV raised \$8 million in November 2012 by selling a 44 per cent stake to UTStarcom Holdings Corp., a publicly listed maker of broadband equipment from China; DeNovaMed recruited a seasoned life sciences executive as CEO; and CarbonCure Technologies signed a licensing deal with Atlas Block to make low-carbon concrete products available in Ontario.
- Throughout 2012-2013, Innovacorp worked towards the creation of a privately operated regional venture capital fund targeting early-stage investment opportunities in Atlantic Canada. The fund manager was named in the fall of 2012 and the fund closed in March 2013. Nova Scotia's \$15-million commitment to the fund was leveraged to \$48.5 million at first close.

2. Maximize the Impact of the Incubation Facilities

Innovacorp manages two incubation facilities and a grow-out facility. The buildings are more than just office, lab and industrial space – they offer an ideal blend of opportunities, resources and synergies that enhance entrepreneurial success.

- In May 2012, Ocean Nutrition Canada (ONC), the primary resident client at Innovacorp's grow-out facility in Dartmouth, was involved in an acquisition. Royal DSM, a Dutch multinational, purchased ONC for \$540 million. Royal DSM continues to occupy the facility and has plans to grow in Nova Scotia. Prior to its move to the grow-out facility, ONC was a long-time resident of Innovacorp's life sciences incubation infrastructure in Halifax.
- Innovacorp secured funding from the Atlantic Canada Opportunities Agency (ACOA) to cover a portion of the fit-up costs at the Innovacorp Enterprise Centre (IEC). The construction will be completed by the end of June 2013, increasing the space available for the province's emerging life sciences and clean technology companies. Twenty per cent of the 42,000 sq. ft. facility remains as green space to be fitted up in 2013-2014.
- Recruitment plans for the incubation facilities were implemented, focusing on the optimal client mix and occupancy level. Frequent tours were provided and a client pipeline document was created to track leads. The recruitment plan resulted in at least three new client companies signing a lease at IEC. In addition, the plan assisted in maintaining the client leases which were renewed during the year.
- Innovacorp collaborated with Dalhousie University, the Capital District Health Authority (CDHA), and other groups to optimize synergies. The purpose was to identify R&D-oriented companies as prospective resident clients for IEC. These collaborations resulted in discussions with the faculty of medicine about allowing IEC clients to access the university's shared research equipment and other resources, and also led to a joint initiative with CDHA that enabled several life sciences companies to get research projects completed by the Saint Mary's University Business Development Centre (SMUBDC). In addition, the strengthened relationships helped us recruit two new resident clients at IEC: ABK Biomedical Inc. and DMF Medical Inc.

- Innovacorp continues to share best practices for incubation with other organizations in Nova Scotia and beyond, to increase successes and maintain a strong brand for the field. Several of our team members are on the Canadian Association of Business Incubation (CABI) board of directors and presented at a boot camp on incubation best practices at CABI's annual conference last fall. In addition, Innovacorp provided guidance on incubation best practices to Acadia University and the Nova Scotia Community College.
- In December 2012, the province announced its intention to develop the former Bowater Mersey mill in Brooklyn (Liverpool) into a centre for demonstrating and piloting cleaner energy, bioresource and forestry innovations. Innovacorp subsequently completed extensive consultations about the centre with industry representatives, researchers, and Southwest Nova Scotia community groups. Specifically, Innovacorp sought to understand opportunities in the bioresource economy as well as industry players' needs so the former mill's infrastructure can be converted into an asset that makes the most of Nova Scotia's forestry resources. The proposed new Innovacorp Demonstration Centre will be an industrial demonstration facility where cutting-edge bioresource industry innovators and researchers can test their products before bringing them to full-market scale.

3. Ensure Access to Globally Competitive Skills, Knowledge and Expertise

Knowledge-based companies seeking to compete internationally require globally competitive business-building expertise. The required expertise ranges from executive leadership to sales and marketing to programming capabilities. There is a shortage of relevant, proven business-building skills available for Nova Scotia start-ups. In 2012-2013, Innovacorp worked to help the province's entrepreneurs access talent and build the skills necessary to grow their ventures.

- Through a variety of initiatives in 2012-2013, Innovacorp continued to enhance its clients' abilities to address the challenges of running a start-up. In addition to our ever-popular Business Over Breakfast series, we offered a half-day workshop on "running lean" facilitated by renowned entrepreneur and author Ash Maurya. Further, we partnered with other organizations to support several Startup Weekends, DemoCamps and Podcamps, and maintained a close working relationship with Entrepreneurs' Forum, including having our vice president of incubation continue to serve as its president.
- In January 2013, Innovacorp recruited another student intern from the Dalhousie University CR MBA program. We added a new twist to the program when we created a Student Entrepreneur in Residence position instead of a traditional internship. We will provide the student with financial support and guidance for his technology venture until August 2013.
- Innovacorp shared its experience and expertise to influence post-secondary curriculum development in the areas of business and strategic planning, entrepreneurship, and commercialization strategies, at several institutions across the province in 2012-2013. For example, we assisted Saint Mary's University (SMU) by providing advice and support in the creation of a new program, Master of Technology Entrepreneurship and Innovation, which kicks off in September 2013. We also participated on the committee to develop the strategic plan for the Sobey's School of Business at SMU.
- In January 2013, we had a full house at the Innovacorp Enterprise Centre (IEC) atrium to hear a presentation from Google Ventures' Daniel Burka, a distinguished product designer, entrepreneur,

start-up advisor and technologist based in San Francisco. The evening also included presentations from two local entrepreneurs, Golnstant's Ben Yoskovitz and TitanFile's Milan Vrekcic.

- We received lots of positive feedback on the governance workshop we held in March 2013. Facilitated by BoardWorks Consulting, the packed full-day gathering focused on start-ups and their boards. Participants commented they felt the workshop was extremely informative.
- In 2012-2013, Innovacorp provided clients with strategic advice in the areas of human resources, marketing and communications. In particular, we played an active role in assisting companies with securing senior talent in the areas of information technology, marketing and sales. A highlight for the year was assisting several former Radian6 employees in landing high-value jobs with a few of our client companies.
- Innovacorp continued to proactively share information with its clients about co-op student opportunities from across all disciplines, bringing value to client and students. In September 2012, we presented comprehensive information on the programs available for student employment as well as the process for hiring co-op students.
- Throughout the year, Innovacorp secured guest speaking opportunities with students at post-secondary institutions, to share stories about innovative Nova Scotia knowledge-based businesses, talk about support available to entrepreneurs, and lead business case study discussions.

4. Maximize Commercialization Potential of Applied Research in Nova Scotia's Post-Secondary institutions

Nova Scotia is home to 11 universities and a strong community college system with 13 campuses across the province. According to Canada's Top 50 Research Universities 2012¹ list, the annual university research income in Nova Scotia, sponsored by government, non-profit organizations and individual businesses, reached \$161.4 million in 2011. Dalhousie University ranked 17th place for research income, with sponsored research income of \$132.5 million. Its research income was 80 per cent of Nova Scotia's total. The Nova Scotia Agricultural College, Saint Mary's University and St. Francis Xavier University ranked 42th, 48th and 49th; their total research income was \$28.9 million.

Furthermore, Canada's Top 40 Research Hospitals 2012² list included two Nova Scotia hospitals. The IWK Health Centre placed 21st with a 2011 research income of \$24.6 million and the Capital District Health Authority placed 28th with \$17.2 million in research income.

While the local economy certainly benefits from the education of students, the attraction of world-class researchers, and the direct and indirect employment generated by post-secondary institutions, the economic benefits derived from applied research continue to be relatively low. Innovacorp has systematically intensified its engagement with post-secondary institutions in recent years and is now supporting and tracking over 60 active projects with high commercialization potential.

- In 2012-2013, Innovacorp managed two successful rounds of the Early Stage Commercialization Fund (ESCF), an initiative designed to assist and support the academic community in pursuit of

¹ Source: <http://www.researchinfosource.com/media/Top%2050%20LR-2012.pdf>

² Source: <http://www.researchinfosource.com/media/2012Top40List.pdf>

entrepreneurial opportunities. Fourteen projects at six institutions were approved for a total of \$500,000 in funding.

- Innovacorp also continued to use its database of research projects in post-secondary institutions to reach out to those identified as having high commercialization potential and invite them to participate in ESCF. Further, ESCF recipients were invited to participate in our info-rich workshops throughout the year.

2012-2013 Financial Results

Summary By Section	Budget 2012-2013 (\$ thousands) ⁽¹⁾	Actual 2012-2013 (\$ thousands)	Variance 2012-2013 (\$ thousands)
<i>Revenue</i> – Nova Scotia funding and operating revenue	\$9,391	\$9,502	111 ⁽²⁾
<i>Operating Expenses</i> – Incubation and Investment	5,899	5,191	708 ⁽³⁾
<i>Corporate Expenses</i> – corporate services, administration, facilities management	2,032	1,992	40
<i>Minus Net Non Operating Items</i> – investment income, interest on long-term debt, post-retirement benefits, amortization	1,601	2,788	(1,187) ⁽⁴⁾
<i>Plus</i> – statutory capital advances re NSFF clean technology fund investments		2,500	2,500 ⁽⁵⁾
Net Income (Loss)	(\$141)	\$2,031	2,172 ⁽⁶⁾

Explanation of Variance

⁽¹⁾ Certain budget line items have been adjusted to align with their presentation in the actual results to enhance comparability of this information.

⁽²⁾ Revenues were higher than budget due to:

- Receipt of \$662K of additional Nova Scotia funding for Early Stage Commercialization Fund awards (\$500K) and Innovacorp Demonstration Centre (\$162K)
- Unbudgeted recovery of regional fund start-up costs incurred (\$171K)
- Incubation revenue higher than planned (\$70K), primarily due to increased rent revenue at the Innovacorp Enterprise Centre

Partially offset by:

- Funding re non-repayable assistance under the clean technology fund under spent (\$860K)

⁽³⁾ Operating Expenses were lower than budget due to:

- Non-repayable assistance provided under the clean technology fund under spent (\$860K)
- \$160K under spent in Incubation due to lower than anticipated Innovacorp Enterprise Centre occupancy costs
- Investment under spent by \$110K primarily due to consulting and salaries
- \$94K under spent on Annapolis Valley office
- I-3 and CleanTech Open follow-up were a combined total of \$65K under spent

Partially offset by:

- Unbudgeted Early Stage Commercialization Fund awards (\$500K)
- Unbudgeted Innovacorp Demonstration Centre costs (\$162K)

⁽⁵⁾ Non-operating costs were higher than budget due to:

- Investment impairments were \$2,685K more than budgeted

Offset by:

- Unbudgeted gain on exit of investment in Golnstant (\$808K)
- Budgets share of regional fund management fees not incurred (\$375K)
- NSFF portfolio earnings were \$222K higher than budgeted
- Unbudgeted gain on Supplementary Employee Retirement Plan settlement (\$101K)

⁽⁵⁾ Under private sector GAAP the receipt of these funds would have been accounted for as a capital transaction. Under the Public Sector Accounting Standards (PSAS) used to prepare these financial statements, contributed surplus is not a recognized element. As a result, these advances are recognized as revenue.

⁽⁶⁾ The significant net income variance arises from the accounting for Statutory Capital Advances described in note 6 above.

Performance Measures

Below is an assessment of Innovacorp's progress towards the performance measures outlined in our 2012-2013 business plan. We continue to review and further strengthen our performance metrics to improve measurement of client progress in building business capabilities, achieving scale and exit potential, and generating return on investment.

The metrics below focus on the areas of economic impact, investment and leading indicators of client-related statistics. Using 2011-2012 as a baseline, these metrics will provide an indication of how well Innovacorp's strategic goals are being met.

Performance Measure: Client company revenue growth

What does this measure tell us?

This measure tracks the annual revenue generated by Innovacorp's portfolio companies (i.e., companies Innovacorp has invested in). An increase in revenue is a key indicator of a company's productivity and overall health.

Where are we now?

In 2012-2013, Innovacorp's portfolio companies generated \$22.1 million in revenue. The vast majority of this revenue was created through exports of products and services outside Atlantic Canada. The revenue is less than the \$30-million target set out for 2012 because Innovacorp invested in several pre-revenue companies in 2012-2013.

Where do we want to go in the future?

We believe that the uncertainty with the economy creates opportunities for entrepreneurs and their knowledge-based companies whose innovations enhance productivity, and therefore forecast that our portfolio companies' revenue will increase to \$30 million in 2013-2014.

Performance Measure: Employment generated by client companies

What does this measure tell us?

This measure follows the annual employment generated by Innovacorp's portfolio companies – a standard measure of economic impact. The ability of Innovacorp's clients to create sustainable employment (and the resulting payroll) contributes to Nova Scotia's economy and indicates a company's progress along the commercialization continuum.

Where are we now?

In 2012-2013, employment generated by Innovacorp portfolio companies was 312 jobs, resulting in \$22.8 million in payroll, exceeding our target for the year.

Where do we want to go in the future?

In 2013-2014, we expect that existing and new Innovacorp portfolio companies will employ approximately 350 people, with \$26 million in payroll.

Performance Measure: Amount of Nova Scotia First Fund (NSFF) leveraged investments

What does this measure tell us?

Innovacorp invests in promising early-stage, knowledge-based companies through the Nova Scotia First Fund (NSFF) to ensure new businesses have the required capital to achieve their full potential at this stage. The leverage metric provides an overall evaluation of Innovacorp's investment strategy by assessing the magnitude by which the corporation's investment capital is leveraged by other investors. Innovacorp tracks the cumulative amount of investment made in NSFF investees, calculating it both as a ratio and in millions of Canadian dollars.

Where are we now?

In 2012-2013, Innovacorp invested \$5.18 million in 12 promising technology companies through the NSFF. These investments leveraged an additional \$6.19 million in investment from financial institutions, strategic and angel investors, and other seed and venture capital funds. The cumulative amount of leveraged investment since 1996 is \$127 million.

Where do we want to go in the future?

In 2013-2014, the target amount of cumulative investment in companies in which investments were made by the NSFF is \$140 million. Our goal is to maintain a leverage ratio of 1:3; and of this additional capital, Innovacorp aims to attract a significant amount from outside Nova Scotia.

Performance Measure: Number of active and new engagements with Nova Scotia-based companies

What does this measure tell us?

Innovacorp's portfolio clients reflect the success and effectiveness of our business model. Continually looking to attract high-potential Nova Scotia companies, we strive to improve the support we offer.

Where are we now?

In 2012-2013, Innovacorp provided business guidance to 130 companies, which was slightly above our target of 120 engagements. The small increase was due to our enhanced focus on providing advice to entrepreneurs in the Annapolis Valley area and on the South Shore, which we achieved through the addition of a Wolfville-based business consultant on our team. In addition to the 130 companies assisted, Innovacorp continued to provide guidance to the majority of 142 companies that made submissions to the provincial I-3 Technology Start-Up Competition the previous year, and worked with a number of university research-level projects that have the potential for later commercial success.

Where do we want to go in the future?

In 2013-2014, we forecast having 140 new engagements with Nova Scotia early-stage knowledge-based companies and making nine new investments. When reviewing this performance measure, it should be remembered that each year it is natural for some portfolio companies to leave the Innovacorp business model and new ones to take their place.

Performance Measure: Number of new clients

What does this measure tell us?

As described above, our client base tells us about the effectiveness of our services and business model. The number of new clients that we form formal relationships with indicates how many early-stage companies we are advancing towards commercial success.

Where are we now?

In 2012-2013, Innovacorp welcomed 10 new portfolio companies (Innovacorp made follow-on investments in two existing portfolio companies), meeting our target for the year.

Where do we want to go in the future?

In 2013-2014, we expect to make nine investments, including a couple of follow-on investments in our existing portfolio.

Performance Measure: Incubation occupancy levels

What does this measure tell us?

Innovacorp's business incubation clients pay market rates for the services we provide and the space they lease in our facilities. Increased occupancy in our incubation facilities results in a larger return on the Province of Nova Scotia's allocation of resources to Innovacorp. However, at any given time, space will be available in our facilities as we achieve our goal of graduating clients into commercial space. While we strive to maintain a high occupancy rate, the turnover of our clients is also a significant positive measure of our performance.

Where are we now?

In 2012-2013, Innovacorp's occupancy rate was 97 per cent at year's end, which was above the target of 85 per cent.

Where do we want to go in the future?

Our goal for 2012-2013 is to have an occupancy rate of about 90 per cent, which is considered to be the best-practice rate for incubation facilities in order to have space available for new clients and existing companies that are ready to expand. Innovacorp will continue to refine the tenant recruitment strategy to ensure that the right mix is achieved.

Performance Measure: Number of clients exporting products/services internationally

What does this measure tell us?

In a relatively small economy like Nova Scotia's, the ability of the private sector to produce and export quality products and services is vital and heavily influences Nova Scotia's economic success.

Where are we now?

In 2012-2013, 92 per cent of Innovacorp's portfolio companies were exporting their products and services. This figure is higher than the target of 90 per cent companies that was set out for the year.

Where do we want to go in the future?

In 2013-2014, our target is to maintain 90 per cent of our portfolio companies exporting their products and services. Several portfolio companies are currently at pre-revenue and we expect the companies invested in will begin to export in 2013-2014.