

2009 Annual Report

HSDC

**HAWAII
STRATEGIC
DEVELOPMENT
CORPORATION**

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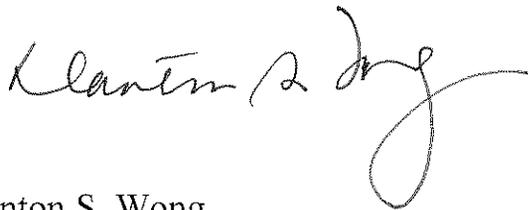
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Message from the Chairman

In these challenging economic conditions and despite a lack of fiscal resources, there is still a need to support the capital formation needs of Hawaii's technology based companies. HSDC, an agency with an independent board and experience managing investment funds, can continue to be a center of excellence for the State as an investor in venture funds or as an administrative agent overseeing the State's financial interests as it pursues economic development polices based on targeted investments in key sectors.

At the end of this fiscal year, we brought on board a new president with experience in private equity investments and HSDC has taken a more active role in managing our investment portfolio. This year's annual report provides an overview of our investment portfolio and investment activity.

We look forward to working with all the stakeholders in Hawaii's technology sector to develop a comprehensive and sustainable program to support innovation, new business formation, and the creation of high wage employment opportunities for Hawaii's citizens.



Danton S. Wong
Chairman of the Board

Message from the President

It is an honor to present my first annual report of HSDC's activities. It has been a challenging several months since joining HSDC and I would like to thank my board and the many people in Hawaii's venture capital community who have helped make my transition into HSDC an enjoyable experience.

This past year, HSDC's board also experienced some transition as Anne Sylvester and Vincent Piekarski stepped down from the board and I would like to thank them for their years of service and contribution. We welcome a new board member, Brian Moore, who brings with him many years of experience managing commercial real estate investment portfolios here in Hawaii.

Looking to the year ahead, the economic environment that confronts Hawaii poses significant challenges, but at the same time creates opportunities for our state's entrepreneurs and venture capital investors. The investment opportunities in Hawaii's clean tech, dual use, life sciences and information technology sectors are as evident as ever, but the ability to raise investment capital to grow these sectors is challenged by a weakened financial system and constraints on the state's fiscal resources.

I look forward to working with Hawaii's venture community to assist them in mobilizing investment capital for the growth sectors of Hawaii's economy. For without continued investment in innovation, the goals of a vibrant and diversified economy will be difficult to meet.



Karl Fooks
President

HSDC's Investment Portfolio

HSDC manages an investment portfolio of approximately \$11.7 million in invested capital. The portfolio has returned \$4.6 million to date and the current carrying value of the investments is \$4.5 million, excluding the \$466 thousand revolving fund balance, but including \$790 thousand of cash awaiting investments held at HSDC Capital Fund, LLC, a fund of funds that is the legal entity through which HSDC holds most of its investments in venture partnerships. HSDC also administers the Follow-on Funding Program, a \$5 million grant program and is the administrative agent for DBEDT's \$8.7 million Hydrogen Fund program.

The overarching purpose of HSDC's portfolio is to 1) support and develop the venture capital industry in Hawaii; 2) support the economic development and diversification of Hawaii's economy by supporting the growth of technology based businesses and 3) support the creation of high wage jobs in Hawaii.

Below is a list of HSDC's active investment portfolio with the amount of capital invested in each fund as of June 30, 2009:

Hawaii-based Venture Capital Funds

HMS Investments; \$2.6 million: Initial investment in September 1995. HSDC holds an 80% limited partner interest in this Hawaii based venture capital investment partnership. The investment portfolio consists of private equity investments in Firetide and Hawaii Biotech.

HMS Hawaii III; \$0.35 million: Initial investment in March 2004. HSDC holds a 12.1% limited partner interest in this Hawaii based venture capital partnership. The investment portfolio consists of private equity investments in Code Factory, Ertek, PingDa, AGIS Network, Sprout, and Firetide. It also holds publicly traded shares of Hoku Scientific.

PacifiCap Hawaii, L.P.; \$3.0 million: Initial investment in June 2000. HSDC holds a 99% limited partner interest in this Hawaii based venture capital partnership. The investment portfolio consists of private equity investments in Fresh Direct Holdings Inc., 4Charity.com, and Trex-Cross Fiber VIPP Note.

Regional Venture Capital Funds

International Venture Fund I; \$4.5 million: Initial investment in April 2000. HSDC holds a 27.01% limited partner interest in this California based venture capital partnership. The investment portfolio consists of private equity investments in Lumidigm, Napo Pharma, AssistGuide, Hawaii Biotech, and Sandpiper Software.

Lava Ventures IV; \$0.5 million: Initial investment in March 2004. HSDC holds an 80% limited partner interest in this California based venture capital partnership. The investment portfolio consists of private equity investments in Nalu Technologies, Three Arch Partners III, Nellix, and TAC Associates.

Technology Gateway Partners II; \$0.5 million: Initial investment in April 2004. HSDC holds a 3.24% limited partner interest in this California based venture capital partnership. The investment portfolio consists of Perlan Therapeutics and Neophotonics.

Fund to Support Hawaii Angels

Heaven Fund I; \$0.075 million: Initial investment in November 2007. HSDC holds a 3.0% limited partner interest in the Series B and Series C of this Hawaii based venture capital partnership. This investment partnership supports investments made by the Hawaii Angels, a Hawaii based Angel investing network and currently holds private equity investments in 20 companies in its investment portfolio.

Fund to Support Technology Transfer from the University of Hawaii

UPSIDE; \$0.093 million: Initial investment June 2003. HSDC holds an 18.75% interest in this pooled capital fund. The balance is held by the Research Corporation of the University of Hawaii. The capital fund is tasked with investing in promising start-up companies using UH developed intellectual property. The investment portfolio consists of private equity investments in Pipeline Micro and Kuehnle Agrosystems and \$380 thousand of cash awaiting investments.

Direct Equity Holdings

HSDC directly holds share certificates, due largely to the liquidation of previous investment partnerships, in the following companies: Neugenesis, Atlantis Cyberspace, DragonBridge Capital LLC, and Nascent Pharmaceuticals. DragonBridge Capital LLC was a direct investment by HSDC. These are all small minority stakes in the respective companies and the aggregate carrying value is \$199 thousand. These values are historical and as these are non-traded shares it is difficult to accurately value these interests.

HSDC is also the administrative agent on two important programs, listed below, promoting the development of technology based companies in Hawaii:

Follow-on Funding Program; \$5 million: The State awarded this grant program to the Pacific International Center for High Technology Research in June 2008. HSDC executed and administers the contract implementing this program with the Pacific International Center for High Technology Research. This is a multi year grant program to support Hawaii technology companies' efforts to commercialize for the civilian market technology originally developed for the military market. \$4.5 million has been provided to 20 projects in Hawaii through a competitive solicitation process. These projects will now be monitored over the next year to help them reach program targets for business development, revenue growth and job creation.

The Hydrogen Investment Capital Special Fund; \$2.6 million: Initial investment in December 2008. HSDC is the administrative agent for this DBEDT managed \$8.7 million program. DBEDT selected Kolohala Ventures to implement this multi year \$4.2 million program to invest in promising start-up ventures that contribute to the development of the hydrogen infrastructure in Hawaii. To date \$2.6 million has been invested in the fund. There is also a \$4.2 million subprogram to provide cost-matching grants to entities in Hawaii pursuing grants for their Hydrogen related projects. To date \$1.2 million has been disbursed.

Financial Report

Revolving Fund (\$000)

HSDC funds its operations and investments through the HSDC Revolving Fund and from returns on investment generated through the HSDC Capital Fund, LLC.

FY Ending	6/30/2007	6/30/2008	6/30/2009
Interest Income/Partnership Distributions	\$44	\$348	\$89
Investments		\$75	\$0
Operating expenditures	\$262	\$229	\$101
HSDC Revolving Fund Balance	\$435	\$479	\$466
HSDC Capital Fund, LLC			
Uncommitted cash awaiting investment	\$845	\$862	\$790

Special Funds (\$000)

Act 240, SLH 2006 established the Hydrogen Investment Capital Special Fund within HSDC, with expenditures to be overseen by the Department of Business, Economic Development and Tourism. The fund was capitalized with \$10,000,000 in October 2006. In June 2009, Act 79, SLH 2009, Sect. 12, transferred \$2,000,000 out of the fund and back to the general fund.

Act 267, SLH 2007 provided \$5 million for the Follow on Funding Program within HSDC.

FY Ending	6/30/2007	6/30/2008	6/30/2009
Hydrogen Investment Capital Special Fund	\$10,033	\$10,493	\$4,839
R&D Follow on Funding Program		\$5,000	\$350

HSDC's Board of Directors

Danton S. Wong, Chairman
Attorney/Partner
Chun Kerr Dodd Beaman & Wong

Eric B. Yee, Vice Chairman
Vice President/Sr. Private Banking Officer
Central Pacific Bank

Jason I. Hauanio
Asst. Vice President, Sr. Financial Advisor
Merrill Lynch

H. Brian Moore
Senior Vice President
Pacific Guardian Life Insurance Co.

Theodore Liu
Director
Department of Business, Economic
Development & Tourism

Roland Resurreccion, AIA LEED
Project Manager
Hawaii Pacific Health
Design and Construction

Darren T. Kimura
President / CEO
Sopogy, Inc.

Glenn S. Yamada
Pearlridge Market Manager
American Savings Bank

Blenn Fujimoto
Vice Chairman, Hawaii Market
Central Pacific Bank
Assumpta Siu Rapoza
Director, Enterprise Risk Mgt.
Hawaii Medical Service Assoc

Edward H. W. Young
TEYC Hawaii

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