DIGIMARC

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Owner Liquidity and Transition

June 2009 • Mike McConnell

Background

Old Digimarc -- $120MM of revenues with 460 employees

- $100MM Secure Credentialing business
  - Principal locations in Boston MA, Fort Wayne IN and Beaverton OR and manufacturing plants in ~ 10 US and foreign locations
  - Produced driver licenses for 2/3 of states in US
  - Produced ID cards (voter, driver license and national IDs) for 25 countries)

- $20MM Digital Watermarking Business
  - Principal location in Beaverton OR
  - Pioneer of digital watermarking
  - Significant Intellectual Patent portfolio: >500 issued and >400 pending

- Shared Services (S/S) business model
  - Legal, Accounting, IT, HR, Marketing & Intellectual Property
  - HQ in OR with staff in MA and IN

"Liquidity Event"

- Sale of Old Digimarc's Secure ID business to L1 Identity Solutions with $310MM going to shareholders
  - Purchased for $56MM in bankruptcy liquidation auction 6 1/2 years earlier
  - Interesting twist:
    - Now being combined with an L1 business unit that came in 2nd place in the bankruptcy auction
    - Resulting combined businesses produce more than 90% of Driver Licenses in the US

- Pre-sale: Spin-off of Digital Watermarking Business into New Digimarc
  - New public company
  - Old Digimarc shareholders receiving new stock
  - 90 EEs, $60MM backlog, $45MM in cash and no debt

Difficult Challenges of Transaction and Resulting Transition

- “Selling” the synergies of acquired business to L-1/Bankers
- “Carved-out” financials for New Digimarc to satisfy SEC From 10 registration process
- Transition Services to L1 and separation of S/S operations

“Selling” the Synergies

- Initial offer @ $250 million: ~1/2 each in cash and L1 Stock to DMRC shareholders
  - “Sell” synergies to L1 management and its banks. L1 was highly leveraged and financing was major variable to close the deal

- SAFRAN, a leading global ID solutions and government systems provider from France raised the ante with a $300MM all cash offer

- L1 topped SAFRAN offer for $310MM cash: to be financed by its banks
  - “Resell” synergies once again to L1 bankers as financing >doubles.
    - Function by function, expense line by line presentation addressing the synergies to be gained from Digimarc S/S operations
    - Identification of synergies and efficiencies to be gained in existing L1 operations once “combination” of division was complete

Carved-out of Financials for New Digimarc

- Form 10 Registration Statement
  - 5 years audited financials required
  - Revenues and COGS data available; separate OPEX records for businesses not maintained for all costs: used “S/S business model”
  - Comprehensive cost allocation methodology employed
    - Grueling collection & identification of data: specific costs identifiable plus various allocation methods employed
  - Received waiver from SEC re: some 2003 and 2004 information:
    - *“Information not available without unreasonable effort/expense”*
    - *“Management believed information not material to the shareholders to gain understanding of the past “carve-out” financial performance and related trends”*
  - “Warning” to reader:
    - “*Financial statements do not include all of the expenses that would have been incurred had the business been a separate stand-alone public entity”*

Transition Services & Separation of Shared Services Operations

Key IT and Finance Challenges

- IT
  - DRMC acting as Co-Lo for L1 acquired operations for ~ one year
  - IT infrastructure split and then rebuilt for New Digimarc from scratch
    - Hardware, software, network, telecom & facilities
- Finance
  - Retaining staff through acquisition date and transition periods
  - Work transitioned from OR to MA & IN
  - G/L split day 1 using transition EEs for both L-1 and Digimarc
  - Shared services for Payroll and A/P continued while L1 staffed up
  - ERP structure duplicated and upgraded to current revs

Current Challenges

- Growing revenues, continuing R&D & limiting losses in current climate
  - Backlog (3X annual revenue) not sufficient to guarantee growth in 2009
  - Disclosed internal target to analysts: achieve revenue growth in 2009
    - But “cautioned” given business climate
  - Increased staff 10%+ to address new business and expanded R&D

- Smaller G&A staff -- wearing many hats – addressing SOX challenges

- Stage is set for achieving financial operating leverage
  - Critical to grow revenues while limiting growth of OPEX
  - Focus in 2009 – efficiency initiatives for IT and finance

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Thank You