Improving life and lifestyle through digital touch interaction

IMMERSION CORPORATION 2000 Annual Report

Computing and Entertainment | Medical | 3D Capture and Interaction | Professional and Industrial

What We Do

Based on Immersion's groundbreaking work in the science of haptics, Immersion's patented TouchSense™ technology enriches people's experience by engaging the sense of touch. Often called the third sense, following sight and sound, touch is a highly refined sensory mode that enables people to intuitively discover, interpret, and understand information.

Today, hardware and software solutions developed with TouchSense technology are being applied to a wide range of digital experiences, including personal computing, entertainment, medical training, automotive interfaces, and three-dimensional (3D) simulation.

The sense of touch can transform an observation into an experience; a spectator to a participant. When you bring touch to a computing environment, it too is transformed. Web sites become more informative and easier to navigate. Games become more electrifying. Computer simulations of medical procedures become powerful means for training surgeons. And automotive controls become features that help drivers stay focused on the road.

Immersion's TouchSense technology provides for a more natural human-computer interaction, making people more productive, software more exciting, simulations more life-like, and interfaces more powerful. And that improved interaction, in turn, can improve people's experience at work, at play, and in their daily lives.
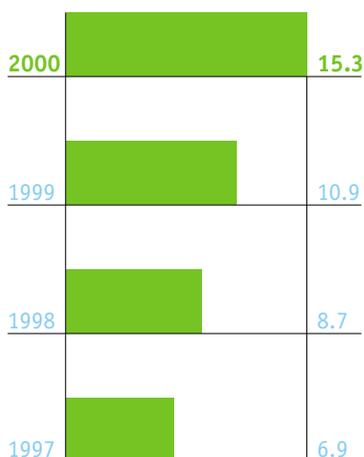
Robert O'Malley
President and CEO

Dr. Louis Rosenberg
Chairman and Founder

Bob O'Malley joined Immersion as President and CEO, bringing more than 25 years of management experience in the computing industry. Dr. Louis Rosenberg, who has served as Chairman, CEO, and President since founding the company in 1993, continues to serve as Chairman and has maintained a full time, active role at Immersion.

Immersion's Revenues

In Millions

Year	Revenue
2000	15.3
1999	10.9
1998	8.7
1997	6.9

Fiscal year 2000 was a time of significant growth and progress for Immersion Corporation. During the year, we expanded our presence, made several strategic acquisitions, sustained market leadership through key partnerships, added critical skills, grew our patent portfolio, and launched a number of exciting new products based on breakthrough technology. All of these achievements have helped to further Immersion's penetration into new and emerging marketplaces, and resulted in record revenues for the year.

Growth in Revenue

Total revenues for the year ended December 31, 2000 increased to $15.3 million from $10.9 million for the year ended December 31, 1999, an increase of 39 percent. Revenue for the year ended December 31, 2000 was comprised of $8.2 million in product sales, which was $2.1 million or 35 percent higher than the product sales for the year ended December 31, 1999; $3.9 million in development contract revenue, which was $1.2 million or 46 percent higher than the development contract revenue for the year ended December 31, 1999; and $3.2 million in royalty revenue, which was $1.0 million or 44 percent higher than the royalty revenue for the year ended December 31, 1999. Pro forma net loss, excluding amortization of intangibles and deferred stock compensation and acquisition related charges, was $13.6 million for the year ended December 31, 2000 or $0.77 per diluted share compared to $6.9 million for the year ended December 31, 1999 or $0.88 per diluted share.

**Immersion's Growing
Patent Portfolio**

Issued U.S. Patents

Year	Patents
2000	39
1999	13
1998	15
1997	10
1996	6
1995	4
1994	1
1993	4
1992	0
1991	0
1990	1
1989	1
Total	**94**

Growing Our Patent Portfolio

Advancing Immersion's intellectual property through patent protection remains a priority for the company and an ongoing strategic initiative. In the year 2000, Immersion and its wholly-owned subsidiaries added 39 U.S. patents to its portfolio, bringing the year-end total to 94. Key patents awarded in 2000 included patents for adding touch technology to the Internet and for enabling the control of multiple automotive systems using the sense of touch. As of year end, Immersion and its wholly-owned subsidiaries had 238 patent applications pending worldwide.

Expansion through Acquisition

The strategic acquisitions of Haptic Technologies Inc., Virtual Technologies, Inc. (VTi), and HT Medical Systems, Inc. have increased our presence in new markets and added valuable human resources, customers, and intellectual property to Immersion.

In March 2000, we completed the acquisition of Haptic Technologies, since renamed Immersion Canada, and gained a wholly-owned subsidiary based in Montreal, Canada. In addition, Immersion acquired a number of Haptic Technologies' issued and pending patents, as well as important hardware and software applications.

The Virtual Technologies acquisition was completed in August 2000 and the company is now a wholly-owned subsidiary of Immersion. With this acquisition, Immersion assumed VTi's portfolio of issued and pending patents in the field of whole-hand sensing, tactile feedback, and real-time 3D-interaction technologies.

In September 2000, we acquired HT Medical Systems, since renamed Immersion Medical. This was an important step in Immersion's growth, increasing our leverage in the growing medical simulation and training marketplace. In addition to the time-to-market advantages of combining HT Medical Systems' recognized expertise in medical procedures and medical simulation with Immersion's leading haptic technologies, this merger resulted in Immersion acquiring several issued and pending medical simulation patents. Now, through leveraged resources, our position in this market is stronger than ever.

These acquisitions not only helped to stimulate our growth and presence in new and emerging markets, they also helped position the Company to better service its expanding customer and partner base.

Building Key Strategic Partnerships

In fiscal year 2000 we achieved a number of major partner milestones. Immersion was pleased to announce the addition of BMW as a TouchSense licensee in 2000. In addition, we saw the introduction of two new tactile mice products, the iFeel™ Mouse and iFeel™ MouseMan®, from our partner Logitech. We signed a middleware partnership agreement with Sony to become a middleware provider for the PlayStation® 2 platform. We licensed our TouchSense technology to Guillemot Corporation to develop new gamepad, steering wheel, and joystick products under Guillemot's ThrustMaster division. And we saw the launch of a new hand-held touch feedback controller — called Panther GTX — by our partner Mad Catz.

New Product Innovation

Since the company was founded in 1993, Immersion has been introducing break-through technologies that touch a variety of applications. This year was no exception. With the introduction of our new 3D scanning product, called LightScribe™-3D, we deployed advanced computer vision technologies to deliver a breakthrough solution for animators, Web developers and designers.

VTi introduced two new products in Q4: CyberForce™ and SimStudio™. CyberForce, a whole-hand haptic glove that provides grounded full-force feedback, complements the existing Cyber family of products. SimStudio enables the creation of realistic 3D software environments.

We also developed and launched the Inertial Harmonic Drive™ technology, which allows for smaller, lower cost, touch-enabled computer devices.

What's ahead for Immersion

We're pleased with progress we made in 2000, the solid growth in all our business units, the strengthening of our patent portfolio, and our proven ability to get into computing markets.

We're excited about the work we're doing to deliver on our long-term goals of strengthening our position as the world leader in the field of haptic technologies and proliferating our TouchSense technology across key markets to ultimately deliver the sense of touch into every office, home, automobile, classroom, and hospital.

Stay tuned for more exciting news about Immersion's haptic technologies in 2001. And thank you for your continued support.
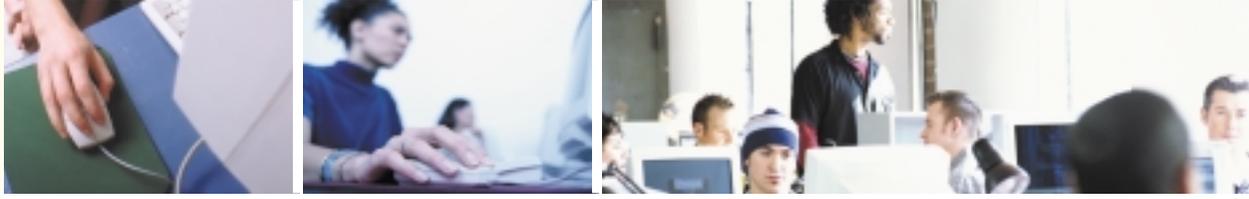
Sincerely,

Robert O'Malley
President and CEO

Dr. Louis Rosenberg
Chairman and Founder

Computing

Enhancing lifestyle through a more intuitive, tactile sensory experience.

"Our Logitech iFeel™ optical mice, which are enhanced by Immersion's TouchSense™ technology, have been a great success since their introduction last September. With their ability to "feel" events within all Windows applications and on the Web, they represent a new dimension in mainstream pointing devices, adding tactile feedback to aid the user as the on-screen landscape becomes more and more complex. Our sales of well over a quarter million units underscores their usefulness."

Wolfgang Hausen
Senior Vice President and General Manager
of the Control Devices Division
Logitech

Computing

Immersion's TouchSense technology is being used by the world's leading manufacturers of computing peripheral devices—including Logitech, Kensington, Primax, Guillemot, and Saitek. These industry leaders are enabling computer users to feel their cursors move around on their desktop; feel the physical forces while using educational, gaming, and entertainment software; and feel their way around a Web page.

Logitech—an international market leader in human interface devices for the PC—has incorporated Immersion's TouchSense technology to enable computer mice products to simulate the sense of touch. Logitech's new family of computer mice, the iFeel™ Mouse and iFeel™ MouseMan, incorporate Immersion's new Inertial Harmonic Drive hardware design and Immersion Desktop software to enable users to "touch" images, objects, and desktop elements displayed on a computer screen. The Inertial Harmonic Drive technology enables realistic tactile feedback from computers in a much smaller physical package and at a significantly reduced cost than previous generations, helping to accelerate the adoption of TouchSense-enabled computer and Web applications. In fact, Logitech shipped over 250,000 TouchSense-enabled units in their first full quarter of sales.

Immersion TouchSense now works with most Web content standards including HTML, Java, and ActiveX controls. In addition, Immersion has formed partnerships with a number of emerging 3D Web standard companies including Hypercosm, Virtue 3D, Geometrix, and Havok, and through such partnerships has been enabling tactile feedback to be added to 3D Web environments. Also, Immersion has enabled support for TouchSense technology within the leading interactive Web standards, including Macromedia's Flash™, Shockwave™, and Dreamweaver® products, allowing Web developers to add compelling touchable content to animated content on the Web. Immersion provides a broad suite of software development tools designed to allow the easy incorporation of touch in a variety of desktop and Web applications. These tools are provided through Immersion's Web Development Kit (WDK) and Software Development Kit (SDK) and easily available to developers on Immersion's Web site.

Screen capture from the game, Black & White.

Entertainment

In the computer games and entertainment market, Immersion is the recognized leader and pioneer of force-feedback technology, as evidenced by our growing community of customers and partners that represent a veritable "who's who" list of industry leaders—including Act Labs, Gravis, Guillemot, Logitech, Microsoft, Saitek, and Sony. Immersion's patented TouchSense technology uniquely enables software and hardware developers to bring realism into the gaming experience by providing real-life tactile sensations for users of joysticks, gamepads, steering wheels, mice, and other game controllers.

By integrating TouchSense technology into their hardware peripherals, and by authoring TouchSense sensations within game software, Immersion's partners are adding high-quality tactile sensations that correspond to events and environments within the computer game world. These sensations add the missing sense of touch to visual and audio effects, bringing a whole new dimension of realism to the gaming experience.

Electronic Arts, one of the world's most respected computer game publishers, is using TouchSense technology to incorporate a fully featured library of tactile sensations into its new release, Black & White from Lionhead Studios. Lionhead was looking to create a breakthrough experience with this game by providing the user with more realism. Using a TouchSense-enabled computer mouse—such as the iFeel Mouse and iFeel MouseMan from Logitech—Black & White users can now feel a wide range of physical sensations that have been incorporated into the game. For example, they can experience the sensation of fish nibbling at their hands as they feed them or of their heartbeat quickening as their spell powers charge.

"In Black & White traditional icons and menus are replaced by an interface that closely resembles our natural interactions in the real-world. We view the Black & White hand as an extension of your own hand. Adding tactile sensations has strengthened that illusion of reality behind the screen."

Peter Molyneux
Managing Director
Lionhead Studios

Improving life by increasing realism and minimizing risk.

Medical

Immersion Medical, formerly HT Medical Systems, is the leader in developing, manufacturing, and marketing medical simulators that recreate realistic healthcare environments.

Historically, the only way for healthcare providers to gain realistic experience was to perform procedures on patients, cadavers, or animals. Immersion Medical's simulators are designed to eliminate these potentially hazardous situations by providing a safer and more humane alternative training method. Using advanced 3D computer graphics, high-fidelity sound, and state-of-the-art tactile feedback, Immersion Medical's simulators virtually reproduce the medical procedure with life-like sight, sounds, and touch sensations.

Immersion Medical produces three comprehensive simulators:

The CathSim® Vascular Access Simulator—developed to train healthcare practitioners and students in intravenous therapy procedures.

The AccuTouch® Endoscopy Simulator—which includes three types of endoscopic procedures:
• Flexible Bronchoscopy, Flexible Sigmoidoscopy, and Colonoscopy.

The AccuTouch® Endovascular Simulator—which allows clinicians to practice endovascular procedures such as pacemaker leads placement, angiography and angioplasty.

Stanford University Medical Center is using Immersion Medical's AccuTouch Flexible Sigmoidoscopy Simulator to train its medical residents in colonoscopy procedures. "The simulation enables us to teach trainees concepts which are very difficult to get across in a lecture," said Jacques Van Dam, M.D., Ph.D., Professor of Medicine at Stanford University School of Medicine and Clinical Chief, Division of Gastroenterology and Hepatology at Stanford University Medical Center. "When trainees use the system, they put their abstract knowledge to use in a realistic and interactive environment," continues Van Dam. "More importantly, they get to make their mistakes on a computer model, not a patient. Their strengths and weaknesses can be assessed objectively before they perform an actual procedure, and their training needs can better be identified. With this system, we can teach without risk, and we will be able to objectively measure clinician competence."

Immersion's TouchSense technology is being used by leading developers of virtual-reality medical and scientific simulations. In addition to developing and marketing its own medical simulation products, Immersion works with a broad range of customers to develop a variety of innovative virtual-reality simulations for procedures such as hysteroscopy, laparoscopy, endoscopy, and others.

3D Capture and Interaction

3D

Through the recent acquisition of Virtual Technologies, Immersion is changing the product design, development, and evaluation process by bringing intuitive, real-time, 3D interaction to the desktop.

VTi, a wholly-owned subsidiary of Immersion Corporation, introduced two exciting new products in Q4: CyberForce and SimStudio. Sandia National Laboratories is a customer of both products, and is looking to use the products to create and interact with simulated 3D CAD models. Sandia has also contracted VTi to perform various development work around these products to explore Sandia's goal of creating a generalized virtual environment.

In the tradition of Immersion's award-winning MicroScribe-3D product line, Immersion's recently announced new product, LightScribe-3D, represents a breakthrough solution for animators, Web designers and developers. LightScribe-3D utilizes advanced computer vision technologies and is licensed exclusively from Geometrix, Inc. LightScribe-3D received the "Innovation of the Year" award by Computer Graphics World Magazine in 2000.

"Combining Geometrix's expertise in advanced 3D capture technology and software with Immersion's strengths in engineering and distribution of 3D content creation products will greatly promote the growth of the interactive 3D Web. Together we are creating a whole new generation of tools that make photo-realistic, touchable 3D Web content possible."

Arthur Zwern
President & CEO
Geometrix

Enhancing lifestyle by engaging the sense of touch.

Automotive

Immersion is pioneering a revolutionary new approach to automotive interface design. By using Immersion's TouchSense technology, manufacturers can consolidate a number of control dials and switches within a single, easy-to-use digital interface that creates a realistic, tactile-based experience for the driver. Working in concert with the dashboard digital display, the Immersion TouchSense enabled automotive system allows for more features to be controlled by a single knob, which can help reduce the number of driver distractions.

"When BMW began development of the 7-series iDrive concept, the challenge was to enable exciting new technologies and features while allowing drivers to stay focused on the road. Immersion's TouchSense technology provided the solution in the form of a programmable controller capable of varying its feel depending on the context of the user interface. This allows a single controller to adjust multiple features and yet retain the distinct familiar feel of the discrete switches and dials it replaces. The result is an intuitive system which offers increased functionality and improved ergonomics."

Hans-Georg Frischkorn
Senior Vice President
BMW

BMW has already licensed Immersion's TouchSense technology to create the automobile industry's first single intuitive control device—called the iDrive™—for use in BMW's new 7 series line of automobiles.

In addition, ALPS Electric, the world's largest electronics components manufacturer, is a strategic partner and preferred supplier of TouchSense enabled controls to the automotive industry. This relationship with ALPS allows Immersion to achieve faster time to market in delivering its haptic technologies to the automotive industry.

"ALPS is always searching for new, innovative products and technologies designed to fit our philosophy of creating a better, safer environment for our customers and the communities they live in. We feel that Immersion's TouchSense technology fits nicely into that philosophy by allowing us to offer our customers technology specifically designed to improve their lives."

Kazuya Yoshikoshi
Director and Manager of the Car Electronics Division
ALPS

Corporate Directory

Board of Directors

Louis Rosenberg, Ph.D
*Chairman and Founder,
Immersion Corporation*

Robert O'Malley
*President and CEO,
Immersion Corporation*

Steven Blank
*Co-Founder and Former Executive
Vice President of Marketing,
E.piphany*

Charles Boesenberg
*Former President and CEO,
Integrated Systems, Inc.*

Jonathan Rubinstein
*Senior Vice President of
Hardware Engineering,
Apple Computer, Inc.*

Corporate Officers

Robert O'Malley
President and CEO

Louis Rosenberg, Ph.D
Chairman and Founder

Victor Viegas
*Vice President, Finance and
Chief Financial Officer*

J. Stuart Mitchell
*Executive Vice President of
Business Groups*

Bruce Schena
*Vice President,
Chief Technology Officer*

Kenneth Martin
Vice President, Engineering

Bhartendu Parekh
*Vice President and
General Manager, Computing and
Entertainment Group*

Craig Factor
General Counsel and Secretary

Corporate Legal Counsel

Heller Ehrman White &
McAuliffe LLP
*275 Middlefield Road
Menlo Park, California 94025*

Independent Auditors

Deloitte & Touche LLP
*60 South Market Street, Suite 800
San Jose, California 95113*

Transfer Agent

BankBoston NA
*c/o Boston Equiserve
150 Royall Street
Canton, Massachusetts 02021*

Stockholder Information

A copy of the Company's Form 10-K, as filed with the Securities and Exchange Commission for the year ended December 31, 2000, is available without charge upon written request to: Immersion Corporation, Attn: Investor Relations, 801 Fox Lane, San Jose, CA 95131. The Company's Form 10-K, other general financial information, and news about Immersion's products are also available on the Company's Web site at www.immersion.com.

Annual Meeting

The Immersion Corporation Annual Meeting of Shareholders will be held June 5, 2001 at 10:00 a.m. at the Silicon Valley Conference Center, 2161 North First Street, San Jose, California 95131.

Market Information— Common Stock

The Company's Common Stock has been traded over-the-counter on the NASDAQ National Market under the symbol "IMMR" since the Company's initial public offering on November 12, 1999.

Corporate Headquarters
801 Fox Lane
San Jose, California 95131
Phone: 408.467.1900
Fax: 408.467.1901
Web: www.immersion.com

Immersion Canada
3575 St-Laurent Blvd., Suite 422
Montreal QC
H2X 2T7 Canada
Phone: 514-987-9800
Fax: 514-987-9808
Web: www.haptech.com

Immersion Medical
55 W. Watkins Mill Road
Gaithersburg, Maryland 20878
Phone: 301-984-3706
Fax: 301-984-2104
Web: www.immersion.com

Virtual Technologies
2175 Park Boulevard
Palo Alto, California 94306
Phone: 650-321-4900
Fax: 650-321-4912
Web: www.virtex.com