



INVESTMENT LETTER  
SOMANETICS CORPORATION (NASDAQ: SMTS)

March 18, 2010

Somanetics Corporation (NASDAQ: SMTS) reported its first fiscal quarter 2010 earnings yesterday. (The company's first quarter ends on February 28, 2010).

**First Quarter Highlights**

- **Net revenues** of \$13.1 million, **up 18 per cent**.
- **Income before income taxes** of \$3.1 million, **up 45 per cent**.
- **Net income** of \$2.0 million, **up 57 per cent**; \$0.16 per diluted share.

In response to this outstanding report, **the shares rose three dollars and sixteen cents** yesterday to **\$20.79**, or a gain of **18.94 per cent** in one day.

Somanetics manufactures a monitor proven to reduce the incidence of brain damage in critical operations, such as the heart bypass procedure.

Somanetics describes its business in its 2009 10 –K filed with the Securities & Exchange Commission, dated February 3, 2010. As you read the following you will get a feeling of why I got very excited when I began to explore the idea of investing in [Somanetics](#):

We develop, manufacture and market the [INVOS System](#), a non-invasive patient monitoring system that provides accurate, real-time blood oxygen measurements in the brain and elsewhere in the body in tissues beneath the sensor in patients greater than 2.5 kilograms (5.5 pounds), and continuously measures changes in blood oxygen levels for individuals of any weight. [The INVOS System is the only commercially available cerebral/somatic oximeter proven to improve outcomes.](#)

The brain is the organ least tolerant of oxygen deprivation. Without sufficient oxygen, brain damage may occur within minutes, which can result in paralysis, other disabilities, or death. Brain oxygen information, therefore, is important, especially in surgical procedures requiring general anesthesia and in other critical care situations with a high risk of the brain getting less oxygen than it needs.

The [INVOS System](#) consists of a portable monitoring system, including proprietary technology, which is used with multiple single-use disposable sensors, called [SomaSensors](#) or [OxyAlert](#) sensors.

[During our fiscal year ended November 30, 2009, net revenues from disposable sensors comprised approximately 81% of our net revenues.](#) As of November 30, 2009, we had an installed base of 2,927 [INVOS System](#) monitors in the United States in 782 hospitals, and during fiscal 2009 we sold 502,026 sensors worldwide.

Clinical studies have shown that using the [INVOS System](#) to monitor and provide information to help manage the regional brain blood oxygen saturation of patients is associated with significantly fewer incidences of major organ dysfunction, which can significantly improve patient outcomes and reduce hospital costs. During fiscal 2004, the



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results of the first prospective, randomized, blinded intervention trial were presented, and the results were published in the January 2007 issue of a peer-reviewed anesthesia journal.

The study showed that when the [INVOS System](#) was used to monitor and provide information to help manage the regional brain blood oxygen saturation of coronary artery bypass surgery patients, the occurrence of major organ morbidity or mortality was reduced from 11% to 3%. Patients with major organ morbidity or mortality have significantly longer lengths of stay in the intensive care unit, or ICU, than those without.

Additionally, in 2004, the results of a large retrospective review showed a statistically significant greater than 50% reduction (2.01% versus 0.97%) in the incidence of permanent stroke when information from the [INVOS System](#) was used to help manage brain blood oxygen saturation of cardiac surgery patients.

Our [INVOS System](#) has U.S. Food and Drug Administration, or FDA, clearance in the United States for use on adults, children, infants and neonates. We target the sale of the [INVOS System](#) for use in surgical procedures and other critical care situations with a high risk of oxygen imbalance.

One of our clients, an M.D. and pathologist who works for Pathology Laboratory Associates, the professional group that manages the Regional Medical Laboratory, Inc., a division of the St. John Health System, suggested, after hearing of my interest in [Somanetics](#), that we meet with Bill Fiddler, Jr., CCP, LP, President of Clinical Perfusion<sup>1</sup> Systems in Tulsa, OK, the highly respected group that does a great deal of the perfusionist work for the St. John Health System.

I met with Bill Fiddler and Ron Lawson of Clinical Perfusion Systems on November 4, 2009 for a discussion about the challenges that a perfusionist faces, particularly during open-heart surgery where monitors, such as the ones that [Somanetics](#) manufactures, are critical in maintaining the correct oxygen blood balance in the brain. Fiddler and Lawson were highly complimentary of the [Somanetics](#) monitor, although they suggested that because of the premium price it would be some time before the company's monitor would become the de facto industry standard.

I left the meeting enthused, noting that two highly experienced perfusionists had a very high opinion of [Somanetic's](#) efficacy. I was not concerned about price because sooner or later, hospital administrators, when considering damage to the brain, would conclude that the time to purchase a [Somanetics](#) monitor was here.

After reading yesterday's press release, I was absolutely certain that [Somanetics'](#) moment had arrived.

The **134,733** shares of [Somanetics](#) that we, the clients, officers, shareholders, and employees of the [Fredric E. Russell Management Co.](#), own represent more than **one percent** of [Somanetics Corporation's](#) **12,907,776** fully diluted weighted average shares outstanding, as of February 28, 2010.

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<sup>1</sup> A perfusionist is a trained health professional who operates the heart-lung machine during cardiac surgery and other surgeries that require the heart and lung functions of the patient to be assumed by a machine. The perfusionist's main responsibility is to support the physiological and metabolic needs of the cardiac surgical patient so that the cardiac surgeon may operate on a still, unbeating heart.