



OPTISCAN IMAGING LIMITED

Annual General Meeting

11 November 2003

ADDRESS BY THE CHAIRMAN, Mr Grant Latta

We have made significant progress in our endeavours to commercialise Optiscan's technology over the past year.

We secured the final Pentax instalment of \$5.5 million, and in the process, positioned the flexible endoscope product for market release in 2004.

We have advanced the process to leverage value from new applications of the technology.

And, as foreshadowed at last year's AGM, we have conducted a thorough re-assessment of the way we operate, and the paths to commercialisation, and we have incorporated these outcomes into a new strategic plan for the company to chart our progress over the coming years.

Before I go into a little more detail on these matters, I would like to recap on the changes that have occurred with the board since the last AGM.

In November last year, two inaugural directors of the company, Dr Alan Finkel and Professor Ray Martin, stepped down from the board, after serving since 1997. In December last year, Matthew Barnett commenced as CEO, and in the same month was appointed a director of the company. In June this year, Martin Harris resigned from the board. Martin was also a founding director, and will continue to serve the company in the area of fundamental research.

I would like to take this opportunity to express my gratitude to the retiring directors for their diligent service to the company

The Board now comprises three non-executive directors, myself as Chairman, Keith Daniel and Tony Rogers. The two executive directors are Matthew Barnett and Peter Delaney. This structure provides a majority of non-executive directors, in line with current practice in this regard.

When we met at the AGM last year, the board gave shareholders an undertaking that there would be a thorough and impartial assessment of the short term and longer-term alternatives available to the company.

The board made this a first priority for the new CEO. In January this year, a detailed review of the company's activities and strategy was commenced. This process resulted in some key outcomes and changes in direction, and represented, in fact, a

defining moment in the short history of the company. It established some fundamental parameters under which the company would move forward.

The first was to declare that that the company would not undertake entry into international markets alone. It must leverage the presence of a partner to gain entry.

The second cornerstone issue to arise from the strategy process was the decision to outsource manufacture and assembly. We formed that view that we are not in a position to make the investment necessary, in both people and infrastructure, to efficiently compete with existing providers of such services.

These outcomes have helped define the emerging shape of our company. We will maintain and enhance our design and development skills; we will subcontract manufacture as necessary; and we will seek partnerships to provide the marketing and expertise necessary to take our technology into the world market.

This focus on our core skill set also enables us to tailor the organisation accordingly. Our overhead and administrative structures have been reduced to the level necessary to support only our core competency of design and development. Implementing the outcomes of this review led to some difficult decisions, including the necessity to let go some loyal and valuable staff, but this was a necessary step in the process of defining the way in which we move forward.

We have maintained our focus throughout the past year on delivering on the Pentax agreement. Whilst this is our most immediate responsibility, we recognise the importance of accelerating our pursuit of new applications in rigid endoscopes and the research market. Matthew will report to you shortly about the detail of this activity, which has been underway since February of this year.

The board accords a high priority to this task. It will become one of the core challenges for the coming year.

The company has always recognised that its real potential lies in establishing a platform technology, from which a range of applications can be developed. The development of flexible endoscopes with Pentax has been a significant achievement, but we must move on to unlock further value from new applications

One could construct a business model based on Pentax flexible endoscopes alone, but such a view would not, in the opinion of the board, fulfil the expectations of shareholders and other stakeholders. The company is therefore of the view that, at a minimum, a second and third application success is necessary to realise the current value in its intellectual property.

At this time, it is expected that these opportunities will arise with rigid endoscopes and instruments for the research market.

For this reason, we expect to maintain our R&D capability and therefore carry the expense in our results. It remains to be seen what level of revenues flow from the release of the Pentax flexible endoscope, but we do not expect that it will be sufficient to recover all of our costs in the first two years from product release. Accordingly, at this time we expect to continue to report trading losses over that period.

Despite the prospect of reporting such accounting results, I trust I have made clear that the priority of the board is to realise the value in our IP. We will be aggressive in our pursuit of new deals, and we will, at all times, give priority to the actions most likely to increase shareholder value in the short term.

Your board believes the company is well positioned and focussed, with its resources now trained on establishing new alliances which build on the base established by the Pentax agreement. These opportunities will be pursued with all our endeavour, because we believe they are the key to unlocking more value in the company.

Before I hand over to Matthew Barnett, I would like to take this opportunity to thank our staff and management for their efforts and contribution over the past year.

It has been a demanding year, with board and leadership changes, re-structuring of operations, staff redundancies and expense reductions. We owe a vote of thanks to our staff who have remained focussed and committed throughout this period of quantum change.

I would also like to express my thanks to Keith Daniel and Tony Rogers, the two non-executive directors, who have provided invaluable support throughout the year. Keith Daniel, in addition to his roles on the audit committee and remuneration committee, has provided the board and management with direction and advice on product development and the path to market, based on his extensive experience in these aspects of the medical device industry.

Tony Rogers is also a member of the Remuneration Committee, and is Chairman of the Audit Committee. Tony has also worked tirelessly throughout the year, providing strong and independent views on management and commercial issues.

I have been demanding of their time over the past year, more so than for most companies of our size, and I take this opportunity to record my appreciation of their efforts.

ADDRESS BY THE CEO, Mr Matthew Barnett

As Grant has outlined, the year since the last Annual General Meeting has been one of significant achievements for Optiscan, positioning us as a leading developer of microscopic imaging technologies for global medical markets.

I would like to start with a quick overview of our business achievements in the 2002/03 financial year.

- We set a new strategic direction for the company that will maximise commercial returns
- We restructured the company's operations and management to focus resources on those activities essential for commercial success.
- We set ourselves seven key milestones to unlock the value of our technology platform and by year-end had successfully delivered two.
- We commenced clinical flexible-endo-microscope trials at Melbourne's Cabrini Hospital.
- We gained very positive market interest from potential users at Pentax's exhibition of the world's first fully functional endo-microscope at Digestive Diseases Week in the USA.
- We directed significant expenditure into areas of core competence but retained a very healthy cash position in excess of \$15M at year-end.
- We secured the final payment under Optiscan's partnership agreement with Pentax, bringing total payments to US\$10m in equity and funding.

Since 30 June 2003 further progress has been made in two critical areas:

- Last month we secured a \$1.4m first order from Pentax, thus completing a third key milestone. This was a company defining achievement and is the culmination of over 1¹/₂ years of intense development work by Optiscan, bringing our technology from concept prototype to sales.
- Working with Pentax we have commenced clinical trials in Germany and Japan designed to scientifically establish the clinical efficacy of our flexible endo-microscope system.

Looking forward, through to the end of the current financial year we expect to:

- Finalise engineering specifications and receive FDA and CE Mark approval for the Pentax flexible endo-microscope
- Assist with Pentax's worldwide market launch of the flexible endo-microscope in early 2004.
- Commence Pentax clinical trials in the USA
- Assist investigating doctors to achieve at least two publications in peer review journals. This is expected to significantly enhance market acceptance and adoption rates of our technology.

- Finalise a path forward for partnerships to pursue the rigid endoscope and research instrument markets

I will now provide some more detail by framing the year in the context of the strategy review we completed in April and then talking about each of the product based markets we are pursuing.

Strategy Review

As Grant outlined this calendar year commenced with your Board and management undertaking a thorough and data intensive review of all aspects of the company's markets, potential markets, operations, capabilities and resources.

We possess a truly unique and market enabling platform technology.

Our now demonstrated ability to miniaturise our scanning technologies to the point where we can fit our high-powered microscopes inside the body has significantly extended our technology's efficacy in medicine.

What our technology platform enables doctors to see for the first time *in-vivo*, will have a significant impact on segments of global medical instrument markets.

The commercial potential for Optiscan from the successful introduction and sales of medical instruments equipped with our technology is now very large indeed.

Through this review process we have also greatly extended our knowledge and understanding of our target markets. We understand their size, structure, concentration and who the key players are.

Importantly we also understand the role new technology introduction plays in their overall development and more particularly in the development of specific businesses. New technology is one of the few means available for participants in these markets to create significant shifts in market share.

Understanding, as we now do, our target markets of medical instruments, our company must, and I stress that we will, work in active collaboration with partners to release the commercial potential of our platform technology.

Our business has a track record of effectively working in partnership with other companies. The Pentax partnership demonstrates that we possess all the core competencies required to find the right partners, develop and consummate well structured licensing and development deals and then deliver to the requirements of those deals.

We believe that this approach to collaborative partnership and its success to-date distinguishes Optiscan from other Australian life sciences companies.

Optiscan's Strategic Direction

Optiscan will pursue a focussed commercialisation of its Intellectual Property, enhancing it and bringing it to market through partners with leading positions in their respective markets

Consistent with this new strategic direction the following actions have been implemented during the last year

- We have restructured the company to provide full focus to the core areas of competence necessary for commercial success, creating annualised savings of \$1.7M.
- We accelerated R&D development timelines and expenditure to meet Pentax deliverables in time for the internationally important congress of Digestive Diseases Week.
- We stopped our expenditure on clinical markets for Stratum.
- We moved to sub-contract the manufacture of sub-systems and components, exiting in-house manufacture in favour of contracting with specialist contract manufacturers.

The identification and pursuit of seven key milestones was a key outcome from the strategy review process.

These key milestones need to be delivered for our company to realise the full value of its platform set of technologies. The full focus on our company is now on meeting these milestones.

Since the time of release of these key milestones in April the company has been, and remains, completely focused on their delivery.

At financial year end the first two milestones of

- Successful exhibition with Pentax of a fully functional flexible endo-microscope at DDW

... and ...

- Receipt of the final payment due under the Pentax development agreement

had been completed on time.

Since June, the milestone number four has also been achieved with receipt from Pentax of an initial \$1.4M order for 20 confocal control boxes and 25 miniaturised scanners.

Receipt of this order was an extremely significant step for our company on the path to commercial success. It demonstrated that we have transitioned to full commercialization of our technology platform.

The remaining four key milestones are at different levels of progression and I will comment further on each later.

Stratum

Many present here today became Optiscan shareholders during the height of the Biotech boom when the company's focus was on the Stratum skin scanner product.

As outlined earlier market realities have resulted in us not pursuing clinical markets for this first generation product.

The instrument itself is being actively and successfully used in clinical research, including a very interesting piece of work on open wound healing, which is being sponsored by the US military.

But this research useage makes adoption into mainstream clinical markets a long way off.

However I must emphasise that Stratum was an important building block for our company

- It demonstrated the application feasibility of our technology into medical instruments and it embodied the first important steps towards miniaturisation for internal body use.
- It taught us valuable lessons about the need to understand market dynamics, customer buying behaviours and the importance of partnerships.
- It served as a valuable prototype platform for the development of the flexible endo-microscope and its existence reduced our development time to market by at least 18 months.

Pentax Flexible Endo-microscope

Close collaboration with Pentax over the last almost two years has seen the joint development of the world's first fully functional flexible endo-microscope.

This has been a truly significant technical achievement with large market potential. It has required us to significantly further miniaturise our scanners and reduce the overall size of the operating system.

All our technical advancements were completed to an accelerated timeline in order to exhibit a fully functional system at the prestigious international congress of Digestive Diseases Week, Orlando, Florida, in May.

Market response from the exhibition was extremely positive with many doctors attending the exhibit expressing their amazement at the clarity of images and the magnification achieved.

Numerous leading research doctors were keen to engage us in discussion about the use of the instrument within their existing research projects.

This excitement was infectious. It was quickly passed from doctors to Pentax sales representatives whose interest was assured by the inability of their competitors to respond to the technology and, of course, their heavily commission based pay structure.

Commercial Framework

The flexible endoscope market at US\$40Mpa is a significant global medical instrument market. It is highly consolidated with Olympus as market leader and Pentax as number two.

Infrastructure and relationships tend to define competition.

Importantly for us, Pentax is implementing a strategy of using new technology to grow its market share.

Pentax is well positioned to be successful with this strategy. They have the dedicated sales channels and the necessary infrastructure to aggressively pursue it.

Our commercial returns from Pentax will come from two key areas

- Royalties - which will be 5-10% of scope final selling price
- Margin on supply of components and sub-systems - which will be 20 – 30%

To make this a little clearer please view the complete Pentax ISC 1000 (Imaging System Confocal) endo-microscope.

A complete system consists of three components:

- A scope. These are made by Pentax. But we supply them with the miniaturised scanner that you can see in the distal tip. Hence for every scope made and sold we earn a margin of between \$2,500 and 4,000 on sale of the scanner component. In addition we receive a 5 –10% royalty on the final selling price, which is expected to be >\$55,000. Each Pentax ISC system will be sold with one or more scopes.
- A video processor box: These are made and sold by Pentax and we have no commercial interest.
- A confocal control box: These are made by Optiscan under sub contract and supplied to Pentax. We earn a margin of between \$13,000 – 18,000 on each one.

The Future

Our immediate priority is delivery of milestone number three, the completion of final engineering specifications. This involves completing Pentax's exhaustive durability and reliability testing and obtaining the required FDA and CE Mark approvals.

While it is a bit unusual to receive an initial order before this engineering work is complete there are some long lead-time items required to manufacture the components we will supply to Pentax and Pentax were keen to ensure that these were ordered in time for their planned market release next year.

Initial sales will come from university / teaching hospitals and selected leading private practitioners.

The joint Optiscan Pentax project committee anticipates sales to build to between 120 and 160 systems pa over the first three years selling to these customers.

This level of sales provides a solid foundation for Optiscan.

However, this level of sales is **not** the end objective for Pentax or for us.

What Pentax and we are excited about is the level of sales that will be obtained if flexible endo-microscopes become **the** "standard of care" for diagnosis and/or treatment of specific conditions or diseases. When this occurs the current base level sales projections will be replaced with significantly higher projections.

Obviously the commercial implications for Optiscan of this occurring are profound.

The vitally important first step towards this outcome is for leading research doctors, using the Pentax flexible endo-microscope, to publish the results of their scientific examinations and demonstrate that an endo-microscope delivers higher standards of patient care and/or more cost effective disease management than a regular endoscope.

This is why the last of our key milestones focuses on publication of successful trial results.

Peter Delaney, our Director of Technology, has the responsibility for working with Pentax's selected leading clinicians in pursuit of these clinical applications. Peter is uniquely qualified to perform this role given his background and his experience with our technology.

Peter could you please give us an overview of the trial activity to date.

Address by Director of Technology, Mr Peter Delaney

As Matthew has introduced, the clinical trial program has to firstly establish the flexible endomicroscope technology in clinical research, and through this activity, establish it as the standard of care in one or more key applications.

Working with Pentax we have commenced an international trial program for our flexible endo-microscope. To date, trials are underway in Mainz University Hospital, Germany, Kyushu University Hospital, Japan, and Cabrini Hospital, here in Melbourne. Further sites are due to start shortly in the USA.

The dual objectives of these trials are to:

- Work with leading doctors to establish effective clinical workflows
- Scientifically establish the clinical efficacy of our flexible endo-microscope system.

Today I would like to update you all on the considerable progress towards these two objectives.

This sequence of pictures best illustrates how our endo-microscope is used clinically.

The images come courtesy of Associate Professor Ralf Kiesslich, who is conducting the trials in Mainz, Germany.

The patient has a known colon cancer tumour which is to be surgically removed.

However, Dr Kiesslich is suspicious of further precancerous changes in numerous tiny lesions around the tumour.

By moving the endoscope closer, he is able to reach a magnification of about 50 times with the normal view of the endoscope. This reveals patterns of small glands, so called "pitts" in the lining of the bowel, but does not allow visualisation of individual cells.

By then moving even closer and touching our endo-microscope onto the lesion, he instantly obtains an image of the cellular makeup of the pitts. Dr Kiesslich is confident that this enables him to diagnose many such lesions quickly and effectively, something that is not practical by current biopsy methods.

He expects that using our instrument will improve his confidence in determining optimal excision margins for tumours and thus reduce the likelihood of recurrence.

Investigating trial site doctors have been impressed with the ability of confocal endoscope to optically section and image beneath the tissue surface. In particular they consider the observation of the microscopic blood vessels and the patterns of sub-surface cell growth to be important differentiators between normal and dangerously abnormal tissue.

This breakthrough magnification and demonstrated useability of our new instrument will underpin sales to the numerous research and teaching hospitals. Pentax's extensive market relationships will facilitate uptake by doctors who are already developing solutions to known medical issues in gastroenterology.

Pentax expects that use in such pragmatic clinical research will lead to establishment of the technology as the future standard of care.

Further, they are sponsoring a number of select international trial sites to scientifically advance those applications believed to have the most medical significance and therefore commercial potential.

Target applications currently under investigation at trial sites are:

- Surveillance of Inflammatory Bowel Disease (IBD) including the common conditions of Ulcerative colitis and Crohn's disease.
- Colon cancer screening, especially detection of flat or non-polypoidal colon cancers which are very difficult to detect and diagnose.
- Surveillance of Barrett's oesophagus which is associated with gastric reflux and can lead to oesophageal cancer. (This is a particularly aggressive cancer facing difficulties in early detection).
- Tumour demarcation and resection margin surveillance in colon and gastric cancers.

Clinical work to date gives us confidence that confocal imaging offers valuable information during colonoscopy in all of the target applications I just listed.

I would now like to give you the details for one of the target applications – detection of "dysplasia" or pre-cancer in patients suffering from inflammatory bowel disease.

Inflammatory bowel disease (or "IBD") includes ulcerative colitis and Crohn's disease. IBD often affect sufferers from quite young in life, but they are chronic conditions, often affecting the patient for life. While short term symptoms include discomfort, pain, diarrhoea and even bleeding, the condition is associated with a long term increase in the risk of developing colon cancer, particularly after years of disease. Patients are therefore advised that they need to have regular (often annual) surveillance colonoscopies after a time so as to offer a good chance of detecting cancer early. In the course of these procedures, it is difficult to see early cancers with the normal endoscope, so biopsies are taken for assessment. If cancer or even a form of pre-cancer termed "high grade dysplasia" is found in the biopsy tissue, then the treatment moves to surgical removal of part or all of the colon.

However there are major limitations with this method. The disease often affects the overall appearance of the colon, so small precancerous changes are often masked to the endoscopist by inflamed or scarred tissue, and small areas of cancer or pre-cancer can be missed.

To offset this problem, a large number of biopsies must be taken, but this too is problematic. It is time consuming, and largely random, especially once several biopsies are taken and bleeding further interferes with targeting of biopsies. However biopsies only sample small regions of tissue – a recent study in Washington found that 33 biopsies would be required to achieve 90% confidence in finding dysplasia, or 66 biopsies to achieve 95% confidence. This is often regarded as impractical, and standard practice is somewhat less than this, and generally involves taking 2-4 biopsies from every 10-20cm of colon affected by the disease.

So, surveillance colonoscopy reduces the risk of early cancer going undetected, but patients cannot be guaranteed certainty, even with annual colonoscopy, and IBD patients have a 2 to 3 fold increased risk of dying from colon cancer. Endo-microscopy is therefore an attractive means to assess the tissue in these patients by rapidly scanning a large number of sites, without removal of large numbers of tissue samples and associated bleeding. At a minimum, it offers the potential to target a small number of better selected sites for biopsy.

So far, trials at Cabrini Monash Academic Surgical Unit in Melbourne, Australia and Mainz University Hospital in Mainz, Germany have begun to scan patients with inflammatory bowel disease. In these example images, tissue in the colon of a patient with Crohn's disease show marked differences from the normal, orderly array of mucous glands observed in normal mucosa.

Early results are encouraging, and the data are being reviewed by the investigators with the help of pathologists to determine the value of the images in finding pre-cancerous or cancerous tissue in inflammatory bowel disease. We are already confident that with confocal endo-microscopy, it is possible to observe more regions of abnormality in a reasonable time than can be found by biopsy.

Investigating doctors are confident that the images hold real value in the detection and differentiation of subtle changes in the mucosa which are impossible to detect macroscopically.

Two manuscripts have thus far been prepared for submission to international peer reviewed scientific journals, with ongoing work expected to lead to further publications. Work has also begun to be presented at international medical conferences.

So, if investigating doctors enthusiasm for this application of the endomicroscope is validated through their scientific studies, the statistics of IBD incidence and management indicate significant sales potential for our systems.

Ulcerative colitis presents 6-15 new cases per 100,000 people each year in western populations, and these numbers are about the same for Crohn's disease. Being a lifetime condition, this amounts to about 60,000 sufferers in Australia and over 1 million sufferers in the USA. Further, the risk of developing colon cancer rises about 0.5% to 1% per year from about 8 years after developing ulcerative colitis or 10-15 years with Crohn's disease.

Thus a significant proportion of sufferers undergo surveillance by annual colonoscopy with multiple biopsies (e.g. several hundred thousand procedures per annum in the USA).

Therefore, with the fees for colonoscopy procedures and pathology services for processing large numbers of biopsies running at several hundred dollars each, IBD surveillance places significant financial burden on western healthcare systems for a result which is not adequate. A time saving procedure with fewer biopsies and

improved detection rates would be an attractive health economic proposition for improving the standard of care in IBD surveillance and cancer prevention.

This is what investigators are working to prove through the trial program.

Of course, the detailed example just presented for IBD represents just one of the specific applications being targeted. Significant progress is being made at all sites.

To date, the Optiscan-Pentax trial program has seen the system used clinically at Mainz University hospital in Germany, where over 60 patients have been imaged (including over 25 cancer patients and 25 IBD patients), Cabrini Hospital here in Melbourne, where 43 patients (including 24 normal, and 19 with bowel disease) have undergone confocal colonoscopy to date, and most recently Kyushu University Hospital in Japan, where 6 gastric cancer patients have been imaged to date.

It is encouraging to witness the international scale on which our partner, Pentax, is able to deploy and raise the profile of our technology. We continue to work actively with Pentax contributing our considerable instrument knowledge to facilitate these trials achieving their objective of scientifically establishing the clinical efficacy of our flexible endo-microscope system

I will now hand back to Matthew to continue this update.

Peter has outlined what I believe are some very encouraging but still relatively early stage clinical findings.

I stress again that should this research show a compelling case for the Pentax endo-microscope to become the "standard of care" for one or more diseases or conditions, then our company's sales base will increase significantly.

That is why publication of clinical trial results is one of our milestones.

Peter and I having spoken at some length about Pentax I now want to turn my attention towards the two major additional commercial opportunities available for our company.

- Securing a partner for rigid endoscope markets
- Securing a partner for confocal microscope research markets

Securing these partnerships are key milestones.

Our development achievements in miniaturising our scanners for incorporation into Pentax's endoscopes means that we now have a strong technology platform.

From our assessment and understanding of potential markets we are confident that we can further commercially exploit our technology further without the need for significant levels of additional R&D.

As Grant explained in his introduction, your Board has determined that the size of these opportunities and the value already present in the technology platform means we should be applying a considerable part of our available cash and people resources to pursue these opportunities as soon as Pentax timelines permit.

Importantly we are now experienced in this partnership forming process and are confident we have the skills required to secure new partnership arrangements.

I want to provide an overview of each market, the opportunity and progress made to date.

Rigid Endoscope Opportunity

The rigid endoscope market at US\$720M pa is not quite as large as the flexible endoscope market. It is however composed of more distinct sub segments and the concentration of market share is not as great as for flexible endoscopes

Unlike flexible endoscopes, which are primarily used for diagnosis, rigid endoscopes are predominantly used for minimally invasive surgical procedures.

We have already engaged discussion with several leading players.

All display strong interest in our technology platform and regard our progress with Pentax as a key point of engagement.

To secure the right partner we are following a three-step process of:

1. Identifying highest value clinical applications based on:
 - Medical need
 - Market size
 - Buyer behaviour
 - Potential partner identification
2. Undertaking clinical pilot investigations with leading clinicians
3. Actively developing business cases for the application that:
 - Define improved care pathways
 - Model practice level and partner economics
 - Develop strategy for achieving coding, coverage and payment

Critical to securing favourable engagement from partners is positive feedback from leading clinicians. Importantly it must be the clinicians that they view as leading – our thoughts in determining who is leading are irrelevant.

This will focus on between two and four specific rigid endoscope applications.

To date we are most advanced in cervical pre-cancer diagnosis.

Clinical trials at Royal Women's Hospital have demonstrated the efficacy of our system to diagnose and grade cervical pre-cancer. We are now working to complete the business case paying attention to defining an improved care pathway for higher-grade abnormalities indicated by pap smear test.

Overall we believe we are in a good position to secure a commercially rewarding partnership. Timing is always hard to estimate when you are dealing with large companies but we have set an internal expectation of having established a firm path forward by June 2004.

Research Market Opportunity

We estimate the global market for research confocal microscopes to be US\$375M pa.

The key for success in this market is the ability of our technology to increase the scientific fields that can be effectively researched with confocal microscopes.

Our unique ability to miniaturise high-resolution scanners makes us believe that we can grow the market for these instruments.

We have also commenced partnership discussions with key participants in this market with a view to forming a partnership.

Again interest has been strong. Business plans inclusive of a thorough assessment of potential research uses for confocal microscopes made possible with our miniaturised scanner technology are currently being prepared by potential partners.

Our internal expectation is to have established a firm path forward by March 2004

Financial Position

A review of our company's financial results shows that we traded at a loss last year.

This reflected the significant expenditure incurred by our R&D team to complete the design, construction and testing of the miniaturised scanners and control boxes needed for key Pentax deliverables.

Importantly, we have maintained a strong cash position throughout the financial year with our closing position for the year remaining above \$15M.

During the first half of this year high levels of expenditure are by the R&D team are continuing in order to complete the engineering required for us to supply the necessary components and sub-systems to Pentax in time for sales release in 2004.

Current cash burn is just on \$0.5M per month with expenditure by the R&D team now representing 56% of total expenditure.

Revenues and margins from the initial Pentax order will appear during the second half of the year but our company will record a loss for the full year and will probably do so again in the following year. Of course, next year's result would change to profit if we concluded a partnership arrangement with an upfront payment component.

Summary

In conclusion, I believe that Optiscan is moved into the commercial phase as an innovative medical technologies company.

We have

- A strong technology and patent position
- Considerable cash reserves
- Focussed management delivering milestones
- Flexible endo-microscope commercialisation starting in 2004 with Pentax, that provides:
 - A sound revenue base, with

- Significant upside available in the event of positive trial results
- Additional commercial opportunities for our technology platform
 - Rigid endoscope markets
 - Research confocal microscope markets

The future holds significant upside for Optiscan.

Value will come from delivery of the remaining milestones.

Your Board, management and staff are fully focussed on delivering these milestones.

I ask that you to measure us by our ability to deliver them.