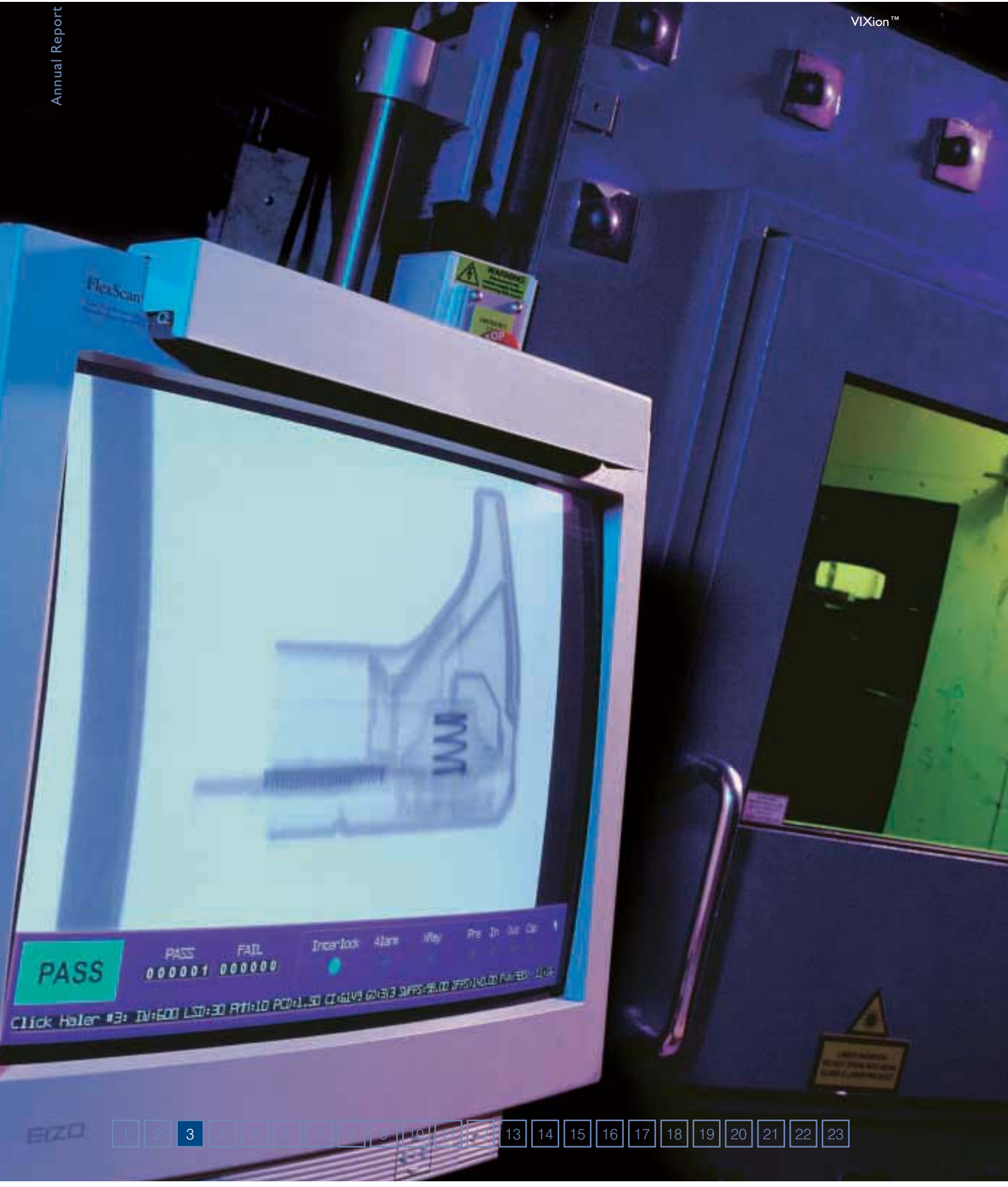


# CREATING A VISION FOR TOMORROW

## REVIEW OF OPERATIONS

VIXion™



## REVIEW OF OPERATIONS CONTINUED



## REVIEW OF OPERATIONS

The key figures in the financial results and the milestones passed during 2001/2 are highlighted in the Chairman's Statement. The increased turnover for last year was derived from three sectoral applications of Image Scan's image capture and image processing technology – security, industrial and medical – each of which is discussed below.

## SECURITY

The Company's range of security products is based upon the 3DX-Camera™, which provides real-time 3D X-ray images for use in the security screening of baggage, packages, freight and cargos at airports, border crossing points, secure buildings, logistics centres and elsewhere. Systems deploying the 3DX-Camera™ and associated software greatly assist screening operatives to assess rapidly the presence or absence of potential threat items within the item under scrutiny.

The second half of the financial year began with a substantial order from the Transport Security Administration (TSA) in America for an AXIS-3D® baggage screening unit, which was delivered during this period. At the same time, the TSA contracted Image Scan to develop a 3D version of Threat Image Projection (TIP) software to run on the AXIS-3D® system. TIP is a software package designed to aid the training and performance monitoring of security screening operatives, by randomly introducing images of threat items (guns, knives, plastic explosive) into the screen being viewed. The 3D TIP software will be made available to the TSA for evaluation during the first quarter of 2003.

In July, we concluded a manufacturing and sales agreement with Rapiscan, a major global manufacturer and supplier of X-ray security screening equipment. Shortly thereafter, the Company secured its first order under this agreement, to deliver a mobile, vehicle-mounted, 3D X-ray security scanning unit to a department of the British Government.

In late October, Rapiscan exhibited the first AXIS-3D® system built jointly by ourselves and Rapiscan at IATA's AvSec World 2002 exhibition in Italy. AvSec World is an important trade fair for the aviation security industry and the AXIS-3D® baggage scanner generated considerable interest from attendees.

## BUSINESS MODEL

Our business model for the security market is either to licence the technology or to act as an OEM supplier of key components, rather than to sell completed systems directly to end-users. Our recent agreements demonstrate the implementation of this model.

## INDUSTRIAL

The industrial inspection systems are designed to facilitate real-time, in-line X-ray inspection of components and assemblies, to ensure conformity with the manufacturer's specification, and to detect and signal any divergence from this. Such industrial inspection applications are particularly relevant if a finished assembly contains concealed working parts, and if the component or assembly is safety-critical, e.g., an electronic automotive component or a drug delivery system.

In May, we signed a memorandum of understanding with Bepak plc (Bepak) and subsequently obtained a research contract with the support of Bepak to explore the use of our VIXion™ multiple view X-ray imaging system to inspect their pulmonary and nasal drug delivery and dispensing products.

For lower resolution applications (up to 0.5mm), we are working on a system incorporating industrialised versions of the 3DX-Camera™, presently used in security systems.

Discussions with potential end-users have led us to identify a market opportunity for a medium resolution industrial inspection system, which is capable of operating at line speeds prevalent in the market. This product was referred to in the Chairman's Statement; provisionally to be known as DEX, it is currently in development and is due to be launched later this financial year.

## REVIEW OF OPERATIONS CONTINUED

### BUSINESS MODEL

In the medium term, the marketing and distribution model for industrial inspection is expected to follow the same strategy adopted for the security market. Initially, however, Image Scan will be working directly with end-users in order to develop a series of highly credible reference sites.

### MEDICAL

Whilst no contributions from medical applications are anticipated for at least three or four years, progress on the innovative cervical smear testing research project has exceeded expectations, and the first laboratory trials are now scheduled for the second half of 2004. Revenue in the year of £67,000 was derived solely from the completion of a first phase research report.

### BUSINESS MODEL

The Company's current policy is to ensure that all research on medical applications of its technology are at least self-funding, owing to the long-term nature of the commercial prospects for such research.

### RESEARCH AND DEVELOPMENT

R&D lies at the heart of Image Scan's commercial potential. The Company's strategy is to identify gaps in existing technology in the market place, to which it believes it can find marketable solutions, either through in-house development, or the integration of externally funded IPR which can be licensed into the Company.

When considering new R&D programmes, the Company will, wherever feasible, seek to minimise both the technical and commercial risk through collaborative research supported with external funding. An example of the practical implementation of this approach, is a research contract awarded in May 2002. This contract, with a total value of £198,000, is to investigate further extending the performance of the Company's VIXion™ system, in addition to developing specific design rules which will enable potential customers to design X-ray inspection capability into their products. This research programme draws on in-house expertise in imaging, X-ray source and detector design, in collaboration with specific key skills from research partners at the University of Bath, Pera and Bespak.



AXIS-3D®

Image courtesy of Rapiscan Security Products Ltd

## REVIEW OF OPERATIONS CONTINUED

The Company maintains close working relationships, both formal and informal, with a number of centres of academic excellence in the UK, Canada and the USA. Included among these organisations are: the Police Scientific Development Branch, Transport Security Administration, The Nottingham Trent University, University College London, Barts & The London Hospital Trust, University of Bath, University of Bristol, Pera and Manufacturing Materials Ontario.

## STAFF AND DIRECTORS

Ian Johnson was appointed a non-executive director at the end of January. He is one of the country's leading security consultants, and has served on many industry and government bodies. He has been an adviser on security to companies such as British Airways and Associated British Ports.

Ray Gibbs joined Image Scan as Finance Director immediately following the admission to AiM. He has helped to reorganise the Company's financial reporting procedures, and his 20 years' experience in practice and industry are proving valuable.

Louise George, the financial controller, has taken on the responsibility of Company Secretary, bringing this function in-house.

Jan Zandhuis became business development manager with specific responsibility for the industrial inspection market in May. He is a highly experienced manager of innovative technology, having held senior posts in the U.K. and continental Europe.

The technical and administrative teams have also been strengthened during the year, and the staff complement is now 16, of whom 12 are technical and 4 in sales or administrative positions.

## FINANCES

The Company raised a total of almost £1.8 million (before costs) of new equity finance during the year and we were therefore able to reduce our indebtedness to a more appropriate level. It is clear, however, that the Company's order book, and the consequent amount of work in progress needed to fund our growth, could rise significantly during the remainder of the current financial year. The average lead-time between receipt and delivery of order for the capital equipment items we provide is 14 weeks, and requirements may therefore arise for working capital funding. With this in mind, the Company has negotiated an additional overdraft facility of £250,000, which may be drawn down as the need arises.

As a result of a number of special one-off contracts, we saw the Company's gross profit margins improve in the second half, from 14.9 percent to 47.7 percent as we concentrated on the delivery of these commercial contracts.

## CONCLUSION

I would like to thank the staff for their support in the year and ongoing commitment to achieving the Group's continued growth and prospects for the future outlined in the Chairman's Statement.



**NICHOLAS D. FOX**  
Chief Executive Officer

16 December 2002