



NAME AND ADDRESS OF SHAREHOLDER

27th February 2004

SHAREHOLDER UPDATE, FROM THE MANAGING DIRECTOR

Dear Shareholder,

With a product launch commencing in April this year and results for the half year to December 2003 being announced to the ASX, it is time to update you on progress with implementing VRI's business plan.

The forthcoming product launch, resulting in pharmacy coverage throughout Australia, marks the transformation of VRI from an R&D company to one with revenue streams building from conversion of our intellectual property to products in mass markets.

Overview

VRI's principal focus is on the global \$5.8 billion pa. probiotic market (*Health Strategy Consulting LLC, 2003*) which according to *Frost and Sullivan 2003* should treble over the next decade. Probiotics are living micro-organisms that provide a health benefit by influencing the intestine and/or by triggering the immune system. A healthy intestinal tract is essential to general well-being.

The company's commercial position is underpinned by patents and technological know-how which allow it to produce high value health products. VRI also has intellectual property in vaccines and diagnostics which have significant potential to be income producing in the near to medium term. These projects will be out-licensed, at the appropriate time, enabling VRI to maintain its focus on probiotics.

VRI's intellectual property is focused on naturally occurring biologicals rather than synthetic compounds, delivering a competitive advantage from shorter lead times in the process of taking natural ingredients from clinical trials to products on pharmacy shelves.

In 2003 VRI completed changes at board and senior management level, relocated the office to Sydney, secured two Government grants totalling \$500,000 to support the vaccine program, and completed two national product distribution agreements. VRI's management team now includes production, marketing and sales people in addition to its R&D team, and is working well with a harmonious Board to execute its business plan. This commercialisation capacity differentiates VRI from most other companies in the Biotechnology sector.

The company is expecting a significant increase to revenue in calendar 2004 with new products in new global markets as well as further progress with developing its product pipeline through its R&D and clinical trials program.

Business plan/strategy

The business plan being implemented by the company has six key elements for building shareholder wealth:

- an immediate focus on *revenue building*, by developing branded products from our patented probiotics technology – the next outcome being the April launch of the ProTractTM product range

- expanding *international distribution* for current products
- reducing *costs*, through collaborative research, contract manufacturing and distribution partnerships
- targeting *market sectors* with high predictive growth rates, from food to OTC and registered pharmaceutical products
- *out-licensing* technologies (diagnostics and vaccines) to development partners better equipped to obtain maximum value
- focusing research efforts on our core competency in probiotics to expand the *product pipeline*

Product launch

In the second quarter of 2004, VRI will launch three TGA listed products under the ProTract brand, each targeting an aspect of intestinal health. The flagship product is a product for the symptomatic relief of *medically diagnosed irritable bowel syndrome* (IBS), a complaint affecting up to 30 per cent of the Australian population and for which no specific treatment or cure is yet available

VRI completed a distribution agreement in November 2003 with CS Pharma, which aims to have the ProTract™ range in 3,000 Australian pharmacies by June 2004.

Revenue from ProTract™ sales will commence during the second quarter.

Building revenue

In 2004 VRI anticipates revenue from at least four sources:

- sales of ProBioPCC™, a dietary supplement for a healthy gastrointestinal environment, being distributed in North America and Asia by Pharmanex.
- sales of Progastrim™, TGA listed and launched in September 2003, with distribution by Life-Span Australia to naturopaths in Australia and NZ. VRI has recently appointed a sales manager to support its marketing
- sales of ProTract™ as outlined above
- sales of the above mentioned products in international markets after registration and as distribution agreements are concluded

Additional events likely to have an impact on revenue over the next twelve months are wider international distribution of the above products and possible sales in the diagnostics and vaccines areas.

VRI has received approval for government assistance, from the Australian government's R&D Start Grant program (\$1 million), BIF grants totalling \$500,000 and Australian Technology Showcase (2004) and, from the NSW Government, over \$200,000 under the BioFirst program. The rigorous approval process involved in the awarding of the grants validates the quality of the company's research.

Board unity

The recent restructure of your board of directors has resulted in a team committed to VRI and enthusiastic about the commercial potential of the company. We now have a board with the

desirable mix of scientific, legal, accounting, marketing and corporate skills working with management to execute a sound business plan.

Financial position

VRI's financial position is sound, with cash reserves at 31 December 2003 of \$2.4 million. Product sales for the half year to December are not directly comparable to the previous corresponding half year because of advance inventory ordering of ProBioPCC™ previously. The most recent half year reflects take up of that inventory by ultimate customers without new distributor ordering although in the current period Pharmanex has placed new orders for distribution in Korea, Japan and Singapore totalling approximately \$500,000 and these orders are in the process of being supplied.

Directors are continually reviewing funding needs for executing VRI's business plan.

Markets

Globally there is an increasing focus on healthy lifestyles and natural ingredients, as well as an ageing population increasingly interested in self care. In commercial terms this is described as the "Wellness" industry. VRI is well positioned to capitalise on these trends since it has developed natural ingredients which have been subjected to clinical trials to prove effectiveness. VRI's active ingredients are also effective as natural additives to various foods, known commercially as functional foods, eg yoghurts and infant formula.

At this stage the company is developing its intellectual property to enhance its commercial potential, with industry statistics demonstrating a market need:

- the total gastrointestinal product market has been estimated at US\$26 to US\$38 billion in 1999, second only to the cardiovascular market (Scrips Report, 2000)
- the global market for probiotic products was US\$5.8 billion in 2002
- IBS, which affects up to 30 per cent of the US population, as in Australia, accounts for 2.4 to 3.5 million physician visits and 2.2. million medical prescriptions in the US annually
- economic impact of IBS in the US is estimated at US\$25 billion annually (American Gastro Assoc) with 19.4 million cases forecast for 2000 (Decision Resources, 2001)

These are just a few statistics which VRI believes make for an attractive and growing market for which we have developed our intellectual property.

Outlook

The board considers there are many positive factors supporting the outlook for your company. We are well positioned commercially and scientifically, to give us access to international markets.

We will report to you as the year progresses and you can look forward to seeing the ProTract range on pharmacy shelves in coming months

Yours sincerely

DR PETER FRENCH
Managing Director