

THE WALL STREET TRANSCRIPT

Connecting Market Leaders with Investors

Viking Systems, Inc. (VKNG.OB)

JOHN KENNEDY was appointed President and Chief Executive Officer, effective Jan. 4, 2010. Previously, Mr. Kennedy served from October 2007 as Viking's President and Chief Operating Officer, as well as a member of the board of directors. Prior to October 2007, Mr. Kennedy was President of the vision systems group at Viking Systems. He joined Vista Medical Technologies, Inc., in January 1997 as Vice President of Research and Development. He was appointed Vice President/General Manager of Westborough Operations in January 2000 before being appointed Executive Vice President and COO in December 2000. Prior to joining Vista Medical Technologies, Inc., Mr. Kennedy held various positions in manufacturing, quality engineering and product development at Smith & Nephew endoscopy from 1984 through January 1997. From 1996 through January 1997, he was the Group Director of Product Development responsible for managing all divisional product development activities. From 1993 through 1996, Mr. Kennedy was Director of Research and Development and was responsible for the management of four technology product development groups. Prior to 1984, he held various engineering positions at Honeywell International Inc.'s electro-optics and avionics divisions. Mr. Kennedy received a B.S. in manufacturing engineering from Boston University in 1979.

SECTOR — HEALTH SERVICES

(AVD608) TWST: Let's start out with a brief overview of Viking Systems, the company's history, products, services and customers.

Mr. Kennedy: Viking Systems is a publicly traded medical device company headquartered in Westborough, Mass. We design and manufacture visualization systems for minimally invasive surgery. Our 2010 revenues were just over \$8 million.

We have two types of products in our business. One is what we refer to as our OEM products, where we manufacture custom cameras, 2D cameras for large blue-chip medical device companies. Companies such as Boston Scientific, Medtronic, B. Braun, Richard Wolf would be the typical company that we would design and manufacture products under with their brand, in our factory. The other product line, the one we are most excited about, is our Viking-branded products. Last October, we launched a new 3DHD visualization system under the Viking brand at the American College of Surgeons' annual meeting. This new product line is intended to replace the current 2D systems used by surgeons today. The Viking 3DHD Vision System enables the surgeon to view and work with the anatomy with a 3D view rather than being limited by their current 2D view. Up until now, the only 3D system available on a large scale had been with the Intuitive Surgical robotic system, the da Vinci. What we have done is deliver to surgeons a comparable standalone vision system. So rather than spending \$1.5 million for the robot, they can have a very similar vision system for on the order of \$100,000 to \$150,000, depending on how the system is outfitted.

We began shipping systems last December, and through March of this year we had shipped 21 distributor-purchased demon-

stration systems, sold 10 end-user systems, and we also installed two systems in academic centers for research purposes. The sales cycle for capital equipment in this price range is typically six to nine months and requires a demonstration in a surgical environment. So getting those demo systems into the market is critical, and we are pleased that our distributors see a big enough opportunity to make a significant investment in the demonstration equipment. We are also happy to have begun receiving end-user orders so quickly and view this as a good trend for things to come.

The product is cleared by the FDA and also carries a CE mark, which allows us to market in the European community. We are actively registering the product in other markets, such as China, and we just recently received approval to market the product in Korea. We view this product launch as a game changer for Viking Systems.

TWST: Would you give us an idea of the size and growth potential of the visualization systems that are currently available?

Mr. Kennedy: Our research indicates that approximately \$2 billion is spent every year on visualization systems to do minimally invasive surgery, and that market is growing globally at about a 3% to 4% rate. That translates globally to between 25,000 to 30,000 vision systems purchased annually. So it's a healthy market, and it's one that we feel that we can have an impact on with our unique technology.

TWST: Please tell us a little bit more about your 3DHD system. What does it do that was not previously available?

Mr. Kennedy: Prior to the launch of the 3DHD system, virtually all standalone vision systems marketed in the United States were 2D systems. In order to see in the surgeons' natural 3D view,

Viking developed a system that captures two HD images simultaneously from slightly different perspectives and displays the 3DHD view in real time on a specially designed 3DHD flat screen display, so the surgeon is looking at a three-dimensional image in high definition resolution, and they're able to see the anatomy in a much more natural format. It has been described as almost being able to put your eyes inside the body and view the anatomy as opposed to current systems, which use only one camera and one optical system. So it is a distinct advantage for the surgeon.

TWST: Who would you describe as your main competition? Who else is doing similar work in this space and what would you say gives Viking an edge over those players?

Mr. Kennedy: The three major players in vision systems for minimally invasive surgery are Stryker, Karl Storz and Olympus. And the primary advantage that we have over all three of those companies is that we are the only one of those companies that offers in the market a 3D visualization system. They all offer 2D, and our niche is the 3D market — which, we believe, we do better than anyone else. Viking has 14 issued patents, five patents pending and other disclosures in the works. So we are very experienced in developing 3D vision for surgeons.

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TWST: As you look ahead at the next several years, at the way the markets will develop, what trends do you see emerging that will help you maintain your focus and position?

Mr. Kennedy: As I said, we are primarily focused on 3D. As procedures become more complex and the instrumentation that's used to perform these procedures becomes more complex, 3D vision becomes even more important. A good example of that is the Intuitive System — the da Vinci robot. You cannot use a da Vinci system without the 3D. It's a critical component of the whole system, and that's because the procedures they're performing are complex and the instrumentation is complex. It moves in multiple angles and planes. And so for the surgeon to be able to understand exactly what is going on with his instrumentation and its relationship to the anatomy he's affecting, it's critically important that he has the depth perceptions.

TWST: Are there any specific near-term opportunities for Viking?

Mr. Kennedy: There are two. The first has to do with improving how procedures are performed. The medical market is always looking to advance or improve how they deliver health care, and we believe that the 3D will allow them to perform more complex procedures in a minimally invasive fashion and a broader audience of surgeons to be able to perform those procedures. The second opportunity has to do with containing or reducing health care costs. An important aspect of this is the investment in a particular technology. While the cost of new technology may seem a little bit higher than the current technology, it is enabling surgeons to perform more complex procedures in the minimally invasive fashion and therefore ultimately reducing the overall cost of health care by converting these to a minimally invasive procedure.

TWST: What about the balance sheet? Do you have the balance sheet in place to follow through on the goals you've set?

Mr. Kennedy: We recently completed a \$3 million financing round led by the Clinton Group. We believe that this provides adequate resources for us to execute our plan as it's laid out today and to reach profitability. Other opportunities that may present themselves farther down the road, either in the product development area or in an M&A situation, may require additional financing. But we'll deal with that as we move forward. Right now, we're laser-focused on delivering the absolute best vision possible to surgeons performing minimally invasive surgery.

TWST: You've only begun selling your system seven, eight months ago. Would you speak to what you're expecting as far as a rate of gain in sales and earnings over the next two years?

Mr. Kennedy: We don't provide specific guidance at this point. What I can tell you is that, in addition to distributor demonstration systems, we started shipping our systems in response to customer orders in December. We sold and shipped three systems in the fourth quarter of last year to end users. We sold and shipped seven end user systems in the first quarter and expect to see continued growth in terms

of system placements. The initial system orders are primarily coming from the international market. The U.S. capital equipment market has a six- to nine-month buying cycle. We have a lot of activity going on in the United States as well as in the rest of the world.

Through March, we have deployed 21 demo systems throughout the world, and this is financed by our distributors who have invested in that demo equipment. In other words, they purchase demo equipment. We don't give our demo equipment to people and hope. We expect our distributors to invest in that equipment. In order to sell vision systems, it does require a clinical demonstration, so they bring the equipment into surgery and demonstrate it and then they go through the business portion of the sales process. For a company our size to have deployed that number of demonstration systems so quickly really demonstrates that these businessmen see the opportunity in their specific markets as well.

TWST: Is there a scenario that could cause higher-than-expected growth or profitability in the future?

Mr. Kennedy: Many different things could happen. Certainly accelerated demand from large institutions or buying groups could accelerate growth. Potential relationships with larger medical device companies or combination technology products, which include maybe robotic or articulating instrumentation combined with 3D, could certainly accelerate the sales of this product, and we are exploring all those avenues.

TWST: Please introduce us to your top-level management team. How would you assess their skill sets and bench strength as you look at opportunities going forward?

Mr. Kennedy: I've been involved in the visualization systems for minimally invasive surgery for 25 years. I started my career with Smith & Nephew, a leader in arthroscopic surgery. I then moved over to

Vista Medical Technologies, where the original 3D development was done. In 2004, Viking Systems acquired Vista. This new system is based on the core competencies that were developed at Vista.

Rob Mathews is our CFO. Rob has many years experience with medical device companies and also a background in public accounting. He worked for Alaris and was instrumental in unwinding a very complex capital structure, which he did here as well. When he came to Viking, we also had a complex capital structure. Now, we have only common stock. We have no debt, no preferred shareholders. It's a very simple capital structure. Rob was also intimately involved with the sale of Alaris to Cardinal Health for \$2 billion. So he's certainly well aware of exit strategies and how they can be executed. Bill Bopp, who is our Chairman, was at Alaris during that same period that Rob Mathews was there. So we certainly have a very strong financial background in the company to navigate the requirements that we operate in the public environment. Recently Yuri Kazakevich has joined the company; it's been about a year now. Yuri is very experienced in the endoscopic optical systems. He's our VP of R&D, a multiple patent holder. And we are building up an even stronger patent portfolio under Yuri's guidance.

TWST: What are the areas you are focusing on personally and why?

Mr. Kennedy: My primary focus is business development. We have two seasoned Vice Presidents managing the sales process. Fred Calnan manages our OEM and international-branded business, and Rob Tierney is managing and developing our U.S.-branded business. Together, the three of us develop and execute the strategies that we believe will maximize our sales and shareholder value. Our number one priority is hospital sales and distributor management — because the proof of the product is its acceptance in the clinical market. If we are successful there, we will demonstrate our true value in the medtech marketplace, which could quite possibly open up larger opportunities.

TWST: In your discussions with the investor community, do you see any recurring questions, any misperceptions?

Mr. Kennedy: I think the single largest challenge we deal with when it comes to investors is our penny stock status. We sure don't consider ourselves a traditional penny stock company. We're an established medical device company. We have revenues. We have ongoing business on a day-to-day basis. Our business is operating, and we happen to have launched a fantastic new product. I think success, in terms of market penetration, is closer than many investors perhaps give us credit for at this relatively early stage.

TWST: As a top manager, what are the ABCs of business according to Jed Kennedy?

Mr. Kennedy: I call it the three Rs: responsiveness, relationships and reliability. That really is the most important thing. While you have to have a great product, you do have to have the relationships with the right organizations. You have to provide a product that's reliable and that addresses a need, and you need to listen to

your customers and respond to what their needs are. These are clearly the most important things, and we live that every day. And that is really how I believe we'll be successful.

TWST: Looking at your financial reports, what are the one or two items that would give a long-term investor a greater insight into the company?

Mr. Kennedy: I think right now the most important number to look at is the top line, the revenue and where that's going quarter over quarter. Our operating expenses are pretty well under control, and we see a need to expand our selling and marketing capabilities. We are right now just in a ramp-up phase where some of the investments we've made in our manufacturing facilities to prepare for the growth are having an impact on where the margins are running right now. But that is strictly a volume issue. As we ramp up production of this product, I think we're going to be very successful.

TWST: What are you utilizing to get the message out to the investor community, and what are your goals?

Mr. Kennedy: Well, we've engaged Porter, LeVay & Rose as our IR firm, and we're doing individual investor meetings at this point — mini roadshows, if you will. The next step is considering which investor conferences to attend to get our story out to a larger audience.

TWST: In conclusion, what would be the three or four summary statements today that would compel an investor to include Viking within their portfolio and within their long-term investment strategy?

Mr. Kennedy: I think that Viking Systems' value proposition today is what it's going to do over the next 12 to 24 months. It appears the company is currently valued on its past history as opposed to future opportunity. So I think there is a real opportunity for people to engage with the company at this point in order to enjoy the benefits that could be realized over the coming 24 months in terms of potential value appreciation. We have a unique technology proposition with a very strong technical group put together to stay ahead of any competition that presents itself. And we have a very solid distribution network. I believe all the key components are in place for a very successful business.

TWST: Thank you. (KL)

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