

Palomar Medical Technologies, Inc. (Nasdaq: PMTI)
2002 Annual Report Highlights



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Dear Shareholders,

We are pleased with our outstanding results over the past year. As compared with the previous year, total annual revenue increased 53% from \$16.7 million to \$25.4 million. Gross margin percentage increased from 32% to 51% and added an incremental \$7.8 million to operating contribution. Even though we increased product and service revenue by 102%, we only increased our operating expenses by a total of 10%. As a result, we improved our bottom line performance by \$5.5 million and posted a profit for the year, while still investing a total of \$4.4 million in research and development.

This profitability is largely due to the enormous popularity of the [Palomar EsteLux™ Pulsed Light System](#). Introduced in September 2001, the EsteLux has proved to be the most multifaceted and affordable light-based aesthetic system on the market. Hundreds of dermatologists, plastic surgeons, spa and salon owners, and other specialists have purchased the EsteLux, which allows them to offer permanent hair reduction, as well as photofacial treatments on vascular and pigmented lesions.

Subsequent Events – The Gillette Agreement

Palomar Medical Technologies capped off this highly successful year by reaching an agreement with The Gillette Company, effective February 14, 2003. Gillette is the leading manufacturer and marketer of blades, razors and shaving preparations for men and women. Gillette's support will assist us in completing the development of a patented, home-use, light-based hair removal device for women. Gillette has the right to commercialize the device worldwide.

Bringing Light-Based Hair Removal to the Mass Market

This agreement with Gillette marks the culmination of a long, challenging process that began in 1996, when Palomar initiated a drive toward the consumer market. It was a risky proposition back then. Lasers at that time were very large, expensive, inefficient, and difficult to operate. As a result, only the most experienced and specialized physician offices could afford or operate these complex early lasers. This left a vast, untapped market of physicians, spa and salon owners, and consumers, which Palomar was determined to reach with light-based cosmetic procedures.

One of Palomar's first goals was to research the technology. To that end, we aligned ourselves with the best clinical research facility in the world, Massachusetts General Hospital, enlisted the support of the opinion makers in dermatology, and assembled the largest multi-center trial for hair removal with some of the best doctors.

These endorsements were critical in validating laser hair removal as a safe and effective treatment. Simultaneously, Palomar built a credible reputation before the FDA, successfully guiding new technologies through the clearance process. Since we began our research and develop-

ment, many of the major advances in light-based hair removal have come from Palomar, including the first permanency label, the first diode laser application, and the first long pulse application.

By 2002, we had made tremendous progress advancing the technology and building a strong patent portfolio. What we lacked was consumer brand recognition, marketing, manufacturing, global distribution, and financial resources for the next phase. We believe our collaboration with Gillette will fill those gaps.

Palomar is confident that the future of hair management lies in light-based treatments. In 2002, consumers worldwide spent an estimated \$2 billion on light-based hair removal. This market is projected to reach \$5 billion by 2007. Palomar has its sights set on capturing a piece of this multi-billion dollar market, and the potentially much larger consumer market, by making our technology available, accessible and affordable to everyone, everywhere.

Lux B™
HANDPIECE

Effective treatment of lighter pigmented lesions on fair skin as well as leg and spider veins.

Lux V™
HANDPIECE

Fast, effective treatment of mild to moderate acne and pigmented lesions.*



*Pending FDA clearance.

Other Achievements of 2002

Palomar has been developing additional enhancements for the EsteLux, including two new handpieces: the LuxV for acne (pending FDA clearance) and pigmented lesions, and the LuxB for lighter pigmented lesions on fair skin, and the treatment of shallow leg and spider veins. These new handpieces join the four previously introduced EsteLux handpieces, which offer permanent hair reduction, among other treatments.

Most importantly, we have introduced a major new product: The **Palomar MediLux™ Pulsed Light System**, an enhanced EsteLux with higher power, faster treatment rate and a snap-on handpiece connector for easy switching between the six handpieces. Positioned as a higher-end option for physicians, the MediLux will complement the lower-priced EsteLux.

Sales of the **Q-YAG 5™ Laser System** continue to gain momentum. This uniquely packaged technology for treating tattoos and pigmented lesions recently received FDA clearance for skin resurfacing. It is the only system on the market with dual, blendable wavelengths for photofacial skin resurfacing, which will be an important application as we move forward.

With new products, new applications, fast-growing sales, and a multi-million dollar development and license agreement with a global marketing and manufacturing giant, we at Palomar feel proud of our achievements and entertain high hopes for the future.

Once again, the management of Palomar wishes to acknowledge the support from our shareholders, employees and directors. Without their support, many of these accomplishments would not have been possible.



Louis P. Valente

Louis P. (Dan) Valente
Chairman of the Board



Joseph P. Caruso

Joseph P. Caruso
Director, Chief Executive Officer
and President

Lux Y™
HANDPIECE

Fastest available hair removal for large body areas, plus pigmented lesion treatment.



Lux R™
HANDPIECE

Fastest available hair removal for all skin types, from the fairest to the darkest, including tans.



Lux Rs™
HANDPIECE

Ultra-concentrated power in each pulse removes hair from all skin types with fewer treatments.



Lux G™
HANDPIECE

Unparalleled photofacial treatments remove vascular and pigmented lesions for rejuvenated skin tone and texture.



Palomar
QYAG 5™
SYSTEM



For tattoo and pigmented lesion removal and skin resurfacing.

Palomar
SUPER LONG PULSE
SLP 1000®



For high-power permanent hair reduction and vascular treatments.

Palomar
ESTELUX™
SYSTEM



For acne, permanent hair reduction and photofacial treatments on pigmented and vascular lesions.*

Palomar
MEDI LUX™
SYSTEM



For high power acne, hair removal and photofacial treatments on pigmented and vascular lesions.*

*Pending FDA clearance.



Palomar Medical Technologies, Inc., 82 Cambridge Street, Burlington, MA 01803
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Palomar MediLux, Lux Y, Lux R, Lux Rs, Lux G, Lux V, Lux B, Palomar Estelux, and Palomar Q-YAG 5 are trademarks, and Palomar SLP1000 is a registered trademark of Palomar Medical Technologies, Inc.

Palomar Medical Technologies, Inc. and Subsidiaries

Consolidated Balance Sheets

	December 31, 2001	December 31, 2002
Assets		
Current assets:		
Cash and cash equivalents	\$5,825,270	\$4,450,076
Accounts receivable, net of allowance for doubtful accounts of approximately \$397,000 and \$554,000 in 2001 and 2002, respectively	2,250,278	4,047,277
Inventories	3,706,828	3,847,493
Other current assets	436,752	269,940
Total current assets	12,219,128	12,614,786
Property and equipment, net	649,691	485,286
Other assets	302,024	298,268
	\$13,170,843	\$13,398,340
Liabilities and Stockholders' Equity		
Current liabilities:		
Debenture	\$500,000	\$ -
Note payable to related party	1,000,000	1,000,000
Accounts payable	1,846,155	1,320,202
Accrued liabilities	4,173,989	4,619,303
Accrued income taxes	1,400,146	1,400,000
Deferred revenue	354,684	341,084
Total current liabilities	9,274,974	8,680,589
Commitments and contingencies (Note 9)		
Stockholders' equity:		
Preferred stock, \$.01 par value-		
Authorized - 1,500,000 shares		
Issued and outstanding -		
6,000 shares at December 31, 2001		
(Liquidation preference of \$8,177,717 as of December 31, 2001)	60	-
Common stock, \$.01 par value-		
Authorized - 45,000,000 shares		
Issued - 11,074,393 and 11,538,706 shares		
at December 31, 2001 and 2002, respectively	110,744	115,387
Additional paid-in capital	163,252,616	162,021,265
Accumulated deficit	(157,368,178)	(157,418,901)
Less: Treasury stock - 573,031 shares at cost at December 31, 2001	(2,099,373)	-
Total stockholders' equity	3,895,869	4,717,751
	\$13,170,843	\$13,398,340

Palomar Medical Technologies, Inc and Subsidiaries

Consolidated Statements of Operations

	Years Ended December 31,		
	2000	2001	2002
Product revenues	\$ 8,781,141	\$ 11,157,770	\$ 22,548,451
Royalty revenues	4,394,462	5,496,034	2,869,085
Total revenues	13,175,603	16,653,804	25,417,536
Cost of product revenues	8,770,931	9,153,090	11,200,077
Cost of royalty revenues	1,757,785	2,198,413	1,147,635
Total cost of revenues	10,528,716	11,351,503	12,347,712
Gross profits	2,646,887	5,302,301	13,069,824
Operating expenses			
Research and development	7,850,599	6,045,343	4,359,346
Sales and marketing	3,153,614	3,504,176	5,785,326
General and administrative	3,865,852	2,491,961	3,066,945
Goodwill and asset write-off	745,804	-	-
Gain from sale of subsidiary	(2,439,556)	-	-
Total operating expenses	13,176,313	12,041,480	13,211,617
Loss from operations	(10,529,426)	(6,739,179)	(141,793)
Interest expense	(155,323)	(98,114)	(119,379)
Interest income	1,203,496	758,938	73,647
Other income, net	380,373	185,786	226,638
Income (loss) from continuing operations before benefit from income taxes	(9,100,880)	(5,892,569)	39,113
Benefit from income taxes	(226,305)	(422,000)	-
Net income (loss) from continuing operations before change in accounting method	(8,874,575)	(5,470,569)	39,113
Cumulative effect of change in accounting method	(712,359)	-	-
Net income (loss)	\$ (9,586,934)	\$ (5,470,569)	\$ 39,113
Basic net income (loss) per share:			
Continuing operations before change in accounting method	\$ (0.90)	\$ (0.54)	\$ -
Cumulative effect of change in accounting method	(0.07)	-	-
Total basic net income (loss) per share	\$ (0.97)	\$ (0.54)	\$ -
Diluted net income (loss) per share:			
Continuing operations before change in accounting method	\$ (0.90)	\$ (0.54)	\$ -
Cumulative effect of change in accounting method	(0.07)	-	-
Total diluted net income (loss) per share	\$ (0.97)	\$ (0.54)	\$ -
Weighted average number of shares outstanding			
Basic	10,246,559	10,805,143	11,372,228
Diluted	10,246,559	10,805,143	11,582,166

Stockholder Information

Stock Price, Dividend and Shareholder Information
Palomar's common stock is currently traded on the National Association of Securities Dealers Automated Quotation System (NASDAQ) under the symbol PMTI. [Go to Stock Chart](#) to view historical stock prices and charts. [Go to Fundamentals](#) to view trading statistics, ratios, balance sheet highlights, cash flow highlights and income statement highlights.

As of February 28, 2003, the Company had 4,682 holders of record of common stock. This does not include holdings in street or company names.

The Company has not paid dividends to its common stockholders since its inception and does not plan to pay dividends to its common stockholders in the foreseeable future. The Company intends to retain any earnings to finance the growth of the Company.

Availability of 10-K's, Quarterly Reports and Proxies
[Go to SEC Filings](#) to view Palomar's filings with the Securities and Exchange Commission, including 10-K's, 10-Q's and proxies.

Shareholders' Annual Meeting

The Annual Meeting of Shareholders will be held on Thursday, May 15, 2003 at 10:00 a.m. at the Marriott Hotel, One Mall Road, Burlington, Massachusetts, 01803.

Directors and Officers

[Go to Management Team](#) to view the biographies and pictures of Directors, Officers, and the Scientific Advisory Committee.

Investor Relations

Palomar maintains investor and shareholder relations programs to keep shareholders and potential investors informed about Company activities. [Go to E-mail Alerts](#) to sign up and receive the latest press releases and information on Palomar as soon as they become available. [Go to Calendar](#) to view dates of upcoming shareholder events such as earnings releases and conference calls/webcasts. We welcome comments and questions from our shareholders. Any time you would like information about Palomar, we encourage you to go to [Info Request](#), email, call or write:

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800-937-5449
www.amstock.com

Independent Auditors

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200 Clarendon St.
Boston, MA 02116

"Safe Harbor" Statement under the Private Securities Litigation Reform Act

With the exception of the historical information contained in this Annual Report Highlights, the matters described herein contain forward-looking statements, including but not limited to statements relating to new markets, development and introduction of new products, and financial projections that involve risk and uncertainties that may individually or mutually impact the matters herein, and cause actual results, events and performance to differ materially from such forward-looking statements. These risk factors include, but are not limited to, results of future operations, technological difficulties in developing or introducing new products, the results of future research, lack of product demand and market acceptance for current and future products, the effect of economic conditions, challenges in managing joint ventures and research with third parties, the impact of competitive products and pricing, governmental regulations with respect to medical devices, including whether FDA clearance will be obtained for future products, the results of litigation, difficulties in collecting royalties, potential infringement of third-party intellectual property rights, and/or other factors, which are detailed from time to time in the Company's SEC reports, including the report on Form 10-K for the year ended December 31, 2002 and the Company's quarterly reports on Form 10-Q. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Company undertakes no obligation to release publicly the result of any revisions to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.