



VITAMINSPICE

From Nutraceutical to Foodceutical

25 FEBRUARY 2010

OTCBB: VTMS

GERMAN WKN: A0YE4L

Company Description

Founded in Pennsylvania in 2008, VitaminSpice has created a new category in the emerging foodceutical industry by combining popular premium common spices with vital daily nutrients, minerals, vitamins, and antioxidants. Through a proprietary patent-pending manufacturing process, the nutritional value of any food is increased with VitaminSpice, which utilizes a recognizable and imaginative alternative delivery system for required daily nutritional intake amounts.

VitaminSpice was the brainchild of founding President and CEO, Ed Bukstel, and originated during an "Ah-Hah" moment with his two daughters while cooking in their Pennsylvania home. His dietary supplement containers had mixed with their cooking spices on the kitchen counter. After eighteen months of product research and development, what followed was an evolutionary line of spices that improved health and wellness by a medium not previously thought to add any benefits to food other than flavor. Three to four servings per day can achieve the recommended daily allowances in various nutrients, and additionally satiate user's palates by appealing to their sense of flavor.

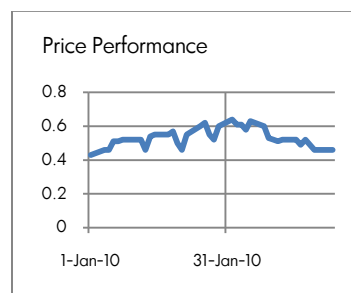
The evolutionary technology consists of premium spice blends (sea salt, ground pepper, granulated garlic, ground cinnamon, crushed red pepper, Italian seasoning) combined with various microencapsulated essential nutrients through taste masking procedures. Nutritional formulas can be chosen based on customer specific needs (cardio, energy, joint, immune, kids, multivitamin) and then microencapsulated to increase the vitamin's stability and heat resistance. During this stage, the vitamins are taste masked and the internal nature is kept intact up to 200 degrees, for maximum cooking use. Thereafter, the microencapsulated vitamin is blended with various spices to complete the process and yield a final enhanced consumer-ready product. Both the spices and microencapsulated vitamin ingredients are Generally Recognized as Safe (GRAS) and undergo multiple random quality control steps throughout the entire process to comply with Good Manufacturing Practices (GMP). The result is an award winning, all-natural, 100% vegetarian, gluten free, calorie free, preservative free, and sweetener free premium spice blend.

A talented and experienced management team leads VitaminSpice. Visionary CEO/founder Edward Bukstel, former Wal-Mart CEO William R. Fields, and Dr Richard Seelig anchor VitaminSpice's board of directors. Mr. Bukstel and Mr. Fields bring valuable experience to VitaminSpice in the areas of health-care information-technology and retail distribution channels, respectively, while Dr. Seelig provides decades of technical acumen to round out the board.

VitaminSpice's unique positioning between the supplement market, the functional food market, and the spice/herb market allows it greater flexibility in capturing market share in three overlapping industries.

Company data

Price(\$)	0.46
Date of Price	25-Feb-10
52-Week Range (\$)	0.28 - 12.00
Mkt Cap (\$ mln)	55.66
Fiscal Year End	Dec
Shares O/S (mln)	121
Exchanges	OTCBB: VTMS German WKN: AOYE4L



Investment Highlights

- Foodceutical market - First mover advantage
- Co-marketing agreements
- Microencapsulation technology
- Alternative vitamin delivery system
- Aging U.S. population
- Private label spice emergence
- Visionary Board of Directors

Investment Risks

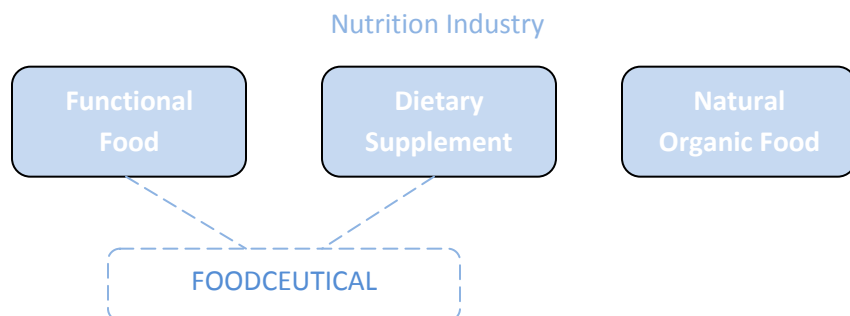
- Slowdown in the U.S. economy
- Highly competitive market
- Raw materials risk
- Operational history

INTRODUCTION

As health and wellness works its way into the fabric of our lives and becomes increasingly popular to the general population, more information emerges about the relationship between health, diet, and lifestyle. Consumers continue to incorporate healthy eating habits into their daily routines with functional foods. However, what is a functional food? U.S. law does not recognize it and there is no consensus definition, but there are a myriad of products in supermarket and high-end grocery store shelves that claim to deliver positive health benefits. Nutrition Business Journal (NBJ) defines it as “food fortified with added or concentrated ingredients to a functional level, which improves health and/or performance, or products marketed for their inherent functional qualities.” More concisely, it refers to any food that provides health benefits beyond the traditional nutrients that it contains.

Functional foods are part of the larger nutraceutical category defined as all dietary supplements, all functional foods, and all organic/natural foods. The term nutraceutical comes from a combination of “nutrition” and “pharmaceutical” referring to foods that act as medicines according to the American Nutraceutical Association. Dr. Stephen Felice coined it in 1989 as “any substance that is a food or a part of a food and provides medical or health benefits, including the prevention and treatment of disease.” Pharmaceuticals are designed specifically for medical use and are subject to Food and Drug Administration (FDA) approval, while nutraceuticals are designed for preventative use and do not require FDA approval.

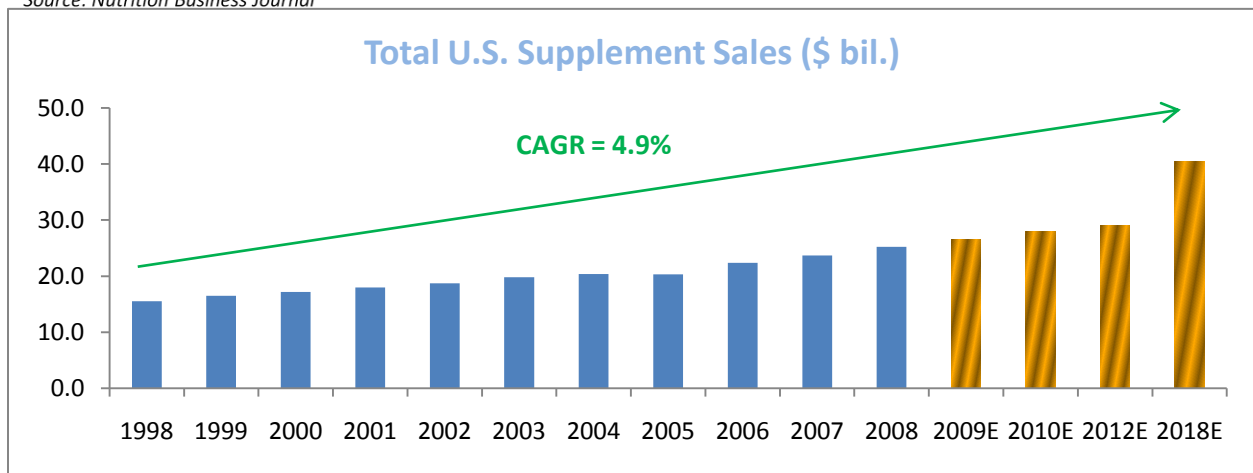
VitaminSpice has created a completely new segment of dietary supplements and is pioneering the emerging foodceutical industry. It can transform any conventional food component (fresh or cooked) into a functional food by combining the benefits of two separate markets, thus, yielding an enhanced, and upgraded product segment. The coupling of commonly used herbs and spices, which inherently possess many intrinsic nutritional benefits themselves, with high quality vitamins, minerals, and antioxidants provides users a flexible, convenient, nutritious delivery system for supplying dietary supplements, multiple times per day.



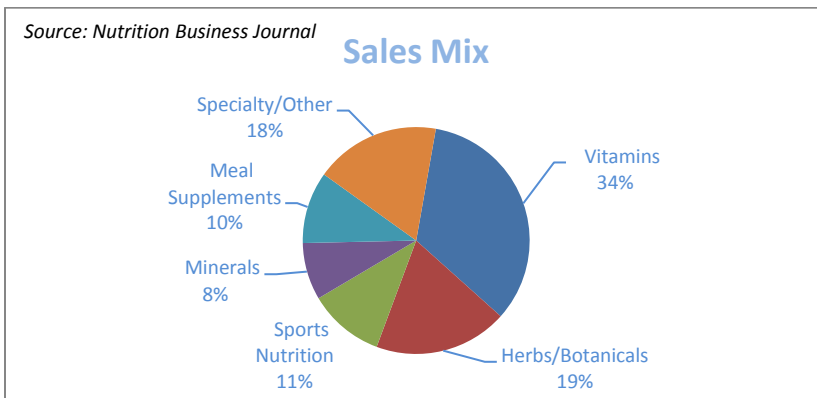
Background on the health food/supplement market

Global sales have maintained mid single digit increases year-over-year as the United States, Western Europe, and Japan comprised over 70% of the supplements industry in 2006. However, sales are still not mature and have more room to grow through 2018. Since 1998, the U.S. supplement industry has grown 63% from \$15.5 billion to \$25.2 billion in 2008 with a CAGR of 5% despite the country's current economic slowdown, according to the NBJ. Growth drivers of this positive industry surge occurred from increased online consumer activity, the aging U.S. population, an increased focus on healthy living, a general shift to prevention from care, and a greater overall acceptance of supplements.

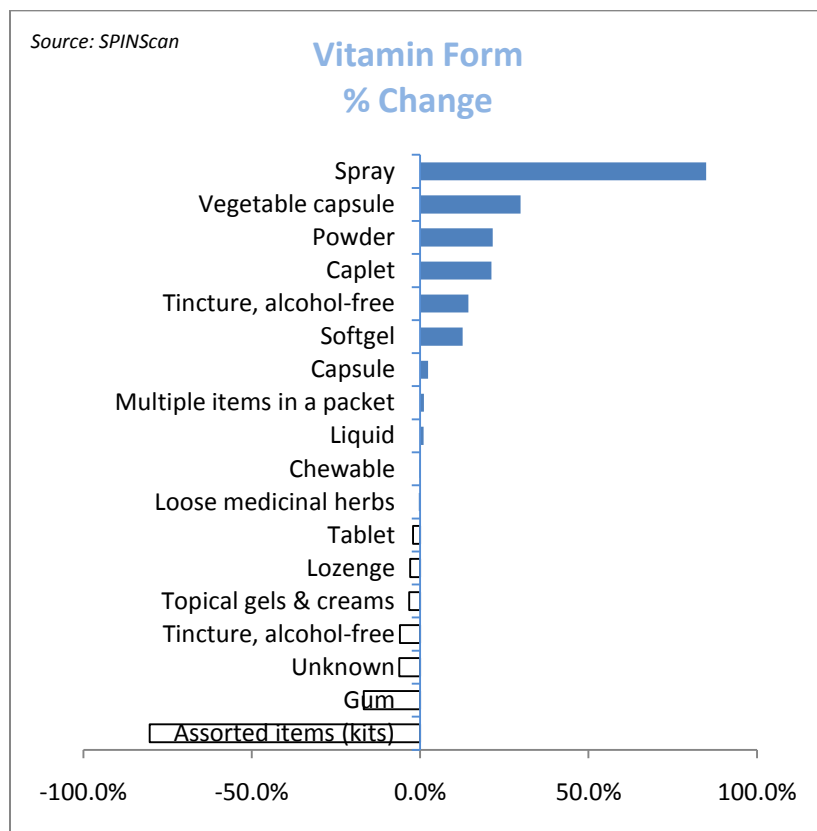
Source: Nutrition Business Journal



Census data estimates that elderly Americans over age 60 are expected to grow three times more than the rest of the population through 2015. In addition, over half of all U.S. adults use vitamins and 34% use vitamins once per day. This bodes well for VitaminSpice as the NBJ found that multivitamin usage increases with age, income, and education levels. Vitamins represented the largest segment of the total industry in 2008 (34%) and were the largest driver year-over-year (9.6%) as well.



In addition, alternate delivery systems for supplements have increased in both sales and the number of products in stores. In 2006, powdered vitamins and minerals increased 51.3% with sales of \$28.9 million in the conventional food, drug, and mass merchandiser channel (FDM). Delivery systems are trending away from traditional pills, driven by a combination of ease of use, ability to mix powders with food or drinks, bioavailability (the fraction of the dose that reaches the system), and higher dosages offered by powdered supplements. According to NBJ, ten years ago only 20% of companies had a liquid or powdered supplement, whereas now it is over 50% because powders have the ability to appeal to consumers who would not otherwise use supplements.



Background on functional food market

The U.S. functional food market is the largest in the world and is expected to have a CAGR of 6.1% from 2007 through 2012. Despite a domestic economic slowdown, there are numerous underlying global trends contributing to the rapid growth of the nutritional industry. Sales that topped \$31 billion in 2006 were driven by the following factors:

- Changing social demographics and increased desire to be healthy
- Aging U.S. population and preventative healthcare
- Young adults aged 15-24
- Consumer awareness that fortified foods can deliver nutritional requirements and have become more receptive to added ingredients (i.e., vitamin D, calcium)
- Media coverage affects sales both positively and negatively
- Safety and contamination scandals
- Obesity and escalating health care costs
- Supplement purchases remain discretionary
- Tightening regulations to offer standardization and eliminate “gray markets”

Some U.S. consumers are opting for functional foods because they have difficulty getting their nutritional daily allowance through traditional foods alone. Increased concerns about health are fuelling interest in certain ingredients known to produce definite benefits. A number of food manufacturers are reformulating new products to introduce healthier alternatives. According to NBJ, consumer awareness of the relationship between food and optimal health has reached an all-time high, showing that 89% of Americans agree that specific foods have benefits beyond basic nutrition and that they may reduce risk of disease. The top functional foods named by consumers are: 1) fruits and vegetables; 2) fish, fish oil, seafood; 3) dairy; 4) meat and poultry; and 5) herbs/spices. In addition, consumers are also associating nutrients with specific health benefits such as calcium and vitamin D for bone health, probiotics for digestion, and antioxidants for free radical protection.

Background on spice industry

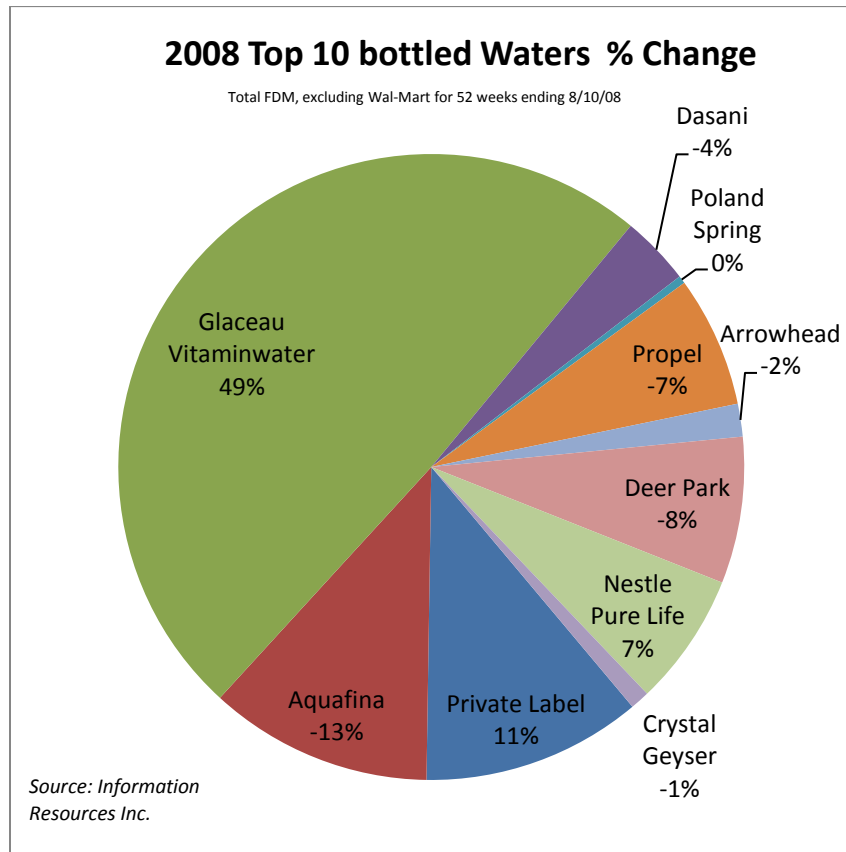
In 1989, the U.S. spice market was worth \$2 billion with major national players occupying shelf space. In 2009, the market was worth \$2.9 billion with private label spices cutting in to national brands market share. Drivers of this trend have been the increase in the acceptance of ethnic foods with various exotic flavors, the decrease of restaurant patronage, and the increase of stay at home chefs. Common spices such as salt and pepper have combined to reach \$392 million in 2007, however their growth has been tempered by rising retail and commodity costs.

Vitaminwater to VitaminSpice

Positioned as a healthy alternative to sugar filled carbonated soft drinks, Vitaminwater grew its roots from a small start-up company that combined regular water with vitamins, minerals, and antioxidants. Acceptance of nutraceutical supplements paved the way for the creation of nutraceutical beverages – ranging

from performance enhancing sports drinks to vitamin and mineral teas and waters.

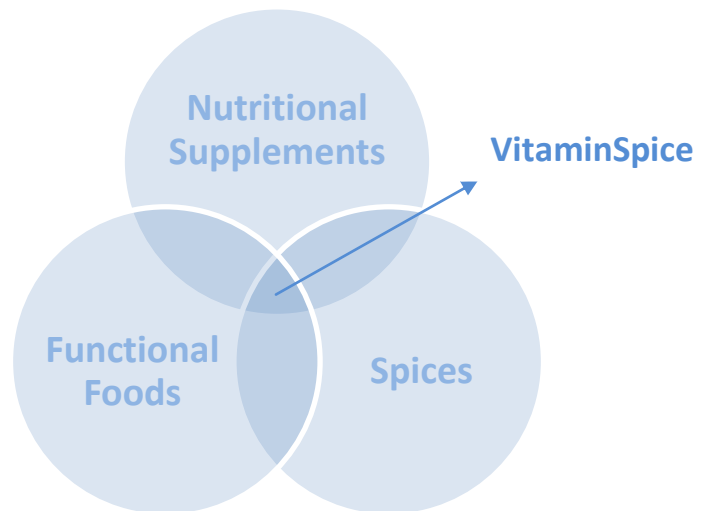
In 1994, Americans were confused and repulsed by drinks containing vitamins and minerals with antioxidants that were specifically designed to be healthy. Consumers had accepted beverages that added no nutritional value except that they tasted good and satisfied their thirst while appealing to their realm of attitude and style. Fast forward to 2010 where the market is so highly saturated with vitamin-enhanced water, sports drinks, and energy drinks which make functional beverages the fastest growing and broadest beverage category with sales just over \$10 billion in 2008. The industry evolved from just water with vitamins to flavored water with fortified juice and as of 2008, the leading functional beverage product was Glaceau's vitaminwater with \$445 million in sales.



Glaceau ballooned from a niche market startup enterprise to a \$350 million mainstream sensation in just 11 years and captured enough market share from the soft drink arena that Coca-cola acquired the company in 2007 for \$4.1 billion. Glaceau's senior vice president Rohan Oza envisioned Vitaminwater as being a "category creator" in the then fledgling \$120 million vitamin enhanced water category in 2002.

Early challenges to Glaceau were developing a pleasing flavor while masking the taste of the vitamins, minerals, and nutrients. This was initially accomplished by adding sugar however, now the balance between sugar and water has evolved to a happy medium – a thin line exists between juice drinks and juice waters. Juice drinks of the past contained vitamins and minerals, but were formulated with excess sugar. Juice waters now are simply juice drinks with not as much juice, and with more water. Water with a hint of juice flavor is now called vitamin water. The category that Glaceau originally helped to create is currently referred to as a functional beverage. These beverages are now characterized as non alcoholic, ready to drink formulations with vitamins, herbs, minerals, amino acids, and fruit/vegetable raw ingredients that satisfy thirst.

Vitaminwater's evolution poses some interesting parallels with VitaminSpice's development: the first mover advantage from conception to production, the consumer trend landscape, and the category creation of an emerging new segment. However, VitaminSpice's encapsulation technology tackles the vitamin flavor issue without adding unnecessary ingredients, contrary to the case of Vitaminwater, which added sugar. Moreover, in the same way that Vitaminwater was an x-factor by adding to the growth of functional beverages, so too, will VitaminSpice add to the growth of nutritional supplements, functional foods, and herbs/spices. Spices with microencapsulated vitamins and minerals opens doors to increased sales that ordinary spices or ordinary vitamins do not. VitaminSpice is a vitamin that tastes good, a spice that nourishes the body, and a functional food category creator – a foodceutical.



SWOT ANALYSIS

VitaminSpice manufactures, markets, and distributes vitamin, mineral, nutrient and antioxidant enhanced spice blends to the retail and institutional food sector. A proprietary micro-encapsulation process taste masks the supplements and protects the flavor of the spices during the production process. Current spice lines include sea salt, ground black pepper, granulated garlic, ground cinnamon, crushed red pepper, and Italian seasoning. Current vitamin formulas include cardio, energy, joint, immune, kids, and multivitamin. These private label products compete for market share in the spice market, the functional food market, and the vitamin/supplement market.

<p>Strengths</p> <p>First mover advantage Co-marketing agreements increase global reach Microencapsulation technology</p>	<p>Weaknesses</p> <p>Operational history</p>
<p>Opportunities</p> <p>Aging Americans Internet sales Shift to private label</p>	<p>Threats</p> <p>Slowdown in the U.S. economy Highly competitive market Raw materials risk</p>

Strengths

First mover advantage

No other company competes in the emerging foodceutical category. The closest product resembling this dynamic was Glaceau's Vitaminwater. By enhancing bottled water with vitamins, minerals, and nutrients, Glaceau successfully captured market share from the then struggling soft drink industry as a healthier alternative to sugar laden carbonated beverages. VitaminSpice provides a recognizable and imaginative alternative to chewable pills, by transforming any conventional food into a functional food. If VitaminSpice can heighten awareness and educate on product benefits, the company will likely see its first mover advantage come to fruition in 2010.

Co-marketing agreements increase VitaminSpice's global reach

The current quantity of co-marketing and co-branding MOU's that VitaminSpice has cultivated could prove to be favorable for geographic expansion. Co-branding agreements with Iron Chef, InterSource Enterprises, Cabo Foods, Heartland Spa, and Christina Pirello should increase VitaminSpice's product awareness and foster heightened distribution.

Microencapsulation technology

VitaminSpice's microencapsulation technology is the catalyst for allowing the company to cross over and affect other markets. By successfully taste masking the ingredients to leave no aftertaste or bitterness it offers users an alternative method for attaining daily nutrient intake levels. In addition, vitamins and minerals are more accepted by consumers because of their familiarity with the ingredients, leading to a comfort level in the natural benefits that vitamins provide, not expecting to feel differently upon taking them.

Weaknesses

Operational history

The company was established in February 2008 and did not have sales until after September 2009. Although VitaminSpice is currently seeking traditional retail distribution channels and expects revenues to rise substantially in 2010, limited amounts of sales have taken place through January 2010.

Opportunities

Aging U.S. population

U.S. consensus data showed that Americans over the age of 60 comprised 17% of the total population in 2006 and that Americans over the age of 65 would increase to 18% by 2025. The amount of Americans over the age of 85 is also predicted to more than double by the year 2030 to 9.6 million. Driven by a shift towards combating rising healthcare costs with more preventative medicines and the push to alternative opportunities in the supplement and nutraceutical segments, VitaminSpice's customer base is likely to grow because of the aging population.

Emergence of private label spices

The spice and herbs market has undergone a shift towards private label products. As of February 2010, Wal-Mart was still considering whether to scale back on branded items in favor of private labels. Private label sales of a basket of U.S. groceries are estimated to have reached 17% in 2009, up from 13% in 1994. VitaminSpice,

which currently operates solely in the private label arena, would benefit greatly from the continued shift away from branded label products during this prolonged U.S. economic slowdown.

Increased internet sales

Online consumer spending has increased over recent years and had sales of \$141 billion in 2008 (Forrester Research Feb 2009) and is projected to boast CAGR of 19.7% through 2017. This is significantly higher than traditional brick and mortar retailing and organic growth of this level provides ample margin potential. Although VitaminSpice has stated that online sales will not be significant in 2010, the online arena proves to be an attractive consumer segment as well as a growing distribution channel.

Threats

Slowdown in the U.S. economy

VitaminSpice's MOU's are mainly in the United States. The U.S. economy has been enduring through a prolonged economic slowdown. Although the acute phase has slightly subsided and a global economic recovery is underway, the recovery is fragile and looks to slow in the bottom half of 2010. The University of Michigan consumer sentiment survey dropped in February 2010 and has been slow to recover since reaching a thirty-year low of 55.3 in November 2008. The purchasing power of VitaminSpice's customers could stifle revenue growth and reduce the company's margins if a rebound in the U.S. economy faltered.

Highly competitive market

VitaminSpice fights for market share in not one, but three different highly competitive industries: the nutritional supplements market, the spices and herbs market, and the functional food/beverage market. Both the nutritional supplements and functional food/beverage markets are highly saturated and fragmented with price, quality, variety, and marketing support driving end-user purchase decisions. The herb and spice market is largely dominated by one company with 50% of the market share. The company competes with public and privately owned companies with larger geographic footprints and broader product portfolios. VTMS competes with nationally branded and private label companies who tend to have greater resources than the company does.

Raw materials risk

Despite prices leveling off somewhat recently, pepper is procured from worldwide suppliers and price volatility may have a negative impact on VitaminSpice's sales and earnings. As of December 31,

2009, black pepper prices were up 46% at \$3,172 per ton from \$2,178 versus the prior year. Global supply of black pepper has declined 2.5% per year since 2003 (with the exception of 2008), according to the International Pepper Community. Reduced output was reported in Indonesia, Brazil, and Sri Lanka. Increased demand and decreased supply has allowed prices to remain at lofty levels. Subsequently, increases in raw materials may adversely affect the company's cost structure and profitability.

Management

Edward Bukstel (Chief Executive Officer/Chief Financial Officer)

Mr. Bukstel has 18 years of experience in the health-care information-technology fields. He has successfully licensed systems and services to companies, including international pharmaceutical and managed care organizations. He was a Vice President at Synetic and CareInsite Corporation (currently WebMD) and holds a Bachelor of Sciences degree from Muhlenberg College. Mr. Bukstel has also completed graduate coursework in Molecular Biology from Temple University.

William R. Fields

Mr. Fields has held numerous Chief Executive positions with various publicly traded companies such as Factory 2-U Stores, Hudson's Bay Company, Blockbuster Entertainment Group (a Viacom division) and with Wal-Mart Stores, Inc., which he joined in 1971. He left Wal-Mart in March 1996 as President and Chief Executive Officer of Wal-Mart Stores Division, and Executive Vice President of Wal-Mart Stores, Inc.

Dr Richard Seelig

Dr. Seelig has been Adjunct Assistant Professor, Medical Informatics Program, at the Nova Southeastern University College of Osteopathic Medicine, and since May 2007, he has been a consultant for the health information technology industry. His duties primarily involved FDA compliance, application development, and market development. Dr. Seelig received a BS from George Washington University and an MD from the New Jersey Medical School and is a Fellow of the American College of Surgeons.

Methodology

A variety of research was examined for the report that included extensive review of secondary literature covering the functional foods market, the nutritional supplements market, the spice market and various industry peers and competitors.

Secondary sources

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