



UNITED-GUARDIAN, INC.

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GUARDIAN LABORATORIES

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Second Quarter 2020 Report to Stockholders

August 31, 2020

Dear Stockholder:

Although the coronavirus epidemic continues to impact the global economies, and has certainly impacted our sales, particularly in China, I am pleased to report that we still had a very profitable second quarter. Net income for the second quarter was up from \$1,078,810 (\$0.23 a share) on net sales of \$3,279,399 in 2019, to net income of \$1,186,611 (\$0.26 a share) on net sales of \$2,954,644 this year. For the first six months of 2020 we had net income of \$1,976,918 (\$0.43 a share) on sales of \$6,277,558, compared with net income of \$2,301,504 (\$0.50 a share) on sales of \$6,459,716 for the first six months of last year.

Some of the fluctuations in net income that we have experienced over the past two years have been the result of a change in accounting rules that was effective in 2018 and required companies to include unrealized gains and losses on marketable securities in net income, even though they may have no correlation with the company's day-to-day operations. While there are many factors that can impact our sales and earnings, this accounting change has resulted in situations where net income decreases even though there is an increase in sales and there are no other cost increases (which is what happened in the first quarter of this year). Similarly, the reverse can happen, like it did in this second quarter. As Warren Buffett of Berkshire Hathaway indicated in a 2017 letter to stockholders: *"The new rule says that the net change in unrealized investment gains and losses must be included in all net income figures. That requirement will produce some truly wild and capricious swings in our bottom-line"*. While those swings in our case are nothing compared with those of Berkshire Hathaway, it can still distort our net income, and this should be kept in mind when analyzing our financial results.

The primary reason for the decrease in overall sales this year has been the lower sales of our cosmetic ingredients, particularly in China. The sales decline in China started shortly after the coronavirus pandemic began, as Chinese companies started to shut down production. Our April sales had been strong because Ashland Specialty Ingredients ("Ashland"), our largest marketing partner and the one that handles our sales in China, purchased additional material to ensure that it had sufficient inventory in the event we had to shut down production. As it turned out, that additional inventory was not needed (since we never shut down), and over the past few months Ashland has been working off that excess inventory. As a result, second quarter sales to Ashland were down by

28%, and 6-month sales to Ashland were down by 11%. When combined with lower sales in Europe, which was due both to the impact of the coronavirus as well as competition from lower-priced products, overall sales of our cosmetic ingredients decreased by 23% in the second quarter compared with last year's second quarter, and 9% for the first six months of the year.

Because of the many uncertainties associated with the coronavirus pandemic, it would be impossible for us to project with any accuracy what our sales of cosmetic ingredients will be for the remainder of this year. It appears that Chinese manufacturers are beginning to reopen, and we are hopeful that this will result in an increase in sales of our cosmetic ingredients in China. Much will depend on the ability of China, Europe, and the U.S. to successfully reopen their economies without significantly increasing coronavirus cases, which could cause companies to shut down again. We are working closely with Ashland and our other marketing partners to ensure that as the global economies reopen they will be ready to supply our customers, and that we will be positioned to be as competitive as possible in order to increase the sales of our cosmetic ingredients.

One bright spot this year has been the revenue from Renacidin Irrigation, the sales of which increased 19% for both the second quarter and the first six-months of 2020, compared with the comparable periods in 2019. We believe that these increases, like those we saw last year, are related to our increased internet presence and advertising. We are continuing to work with our internet marketing consultant to monitor this program, and we are optimistic that we will continue to see increases in Renacidin sales as that marketing campaign continues. I would also like to note that recently we were able to negotiate and finalize a 5-year renewal of our contract with the Department of Veterans Affairs (VA), which will enable us to continue to supply Renacidin to the VA and its patients.

In regard to new product development, here is an update on some of our current projects:

- **Lubrajel Marine:** this is a formulation of Lubrajel that was developed using naturally-derived polysaccharides, with some of the ingredients sourced from marine vegetation. The original formulation of this product is already on the market, with sales increasing gradually. We have been working with Ashland on a new product of theirs that incorporates into Lubrajel Marine a low-cost active ingredient made by Ashland. The coronavirus delayed the marketing of this product, which was scheduled to be introduced by Ashland this past spring. Ashland is very enthusiastic about this product, and they are now expecting the product launch to take place in November.
- **Lubrajel Oil Natural:** this is a natural version of our very popular Lubrajel Oil. It was developed using vegetable feedstock and, like Lubrajel Marine, is based on polysaccharide chemistry. Like our other "natural" products, this product has been certified by Ecocert to comply with COSMOS standards for use in natural and organic cosmetic products. Sensory testing has now been completed, and hydration testing will be done during the winter months when it is more accurate. We anticipate that this product will be ready for sampling to our global marketing partners early next year.
- **Lubrajel Oil PF:** this is a preservative-free version of Lubrajel Oil that has already been sampled by Ashland to over two hundred customers in China. Like so many other things, the coronavirus significantly impacted the timetable for the introduction of this product, but the formal launch is expected to take place by webinar in the next few months.

- **Lubrajel II XD PF:** This is a modification of Lubrajel II XD, one of our higher-viscosity Lubrajels, which we have now formulated to be preservative free. Ashland believes that there may be significant interest in this product, particularly in Korea where preservatives are an issue. We are hoping that this product will enable us to recover and rebuild the business we previously had in Korea. There is also a new sales opportunity for this product in Europe, where we may be able to replace one of our competitor's products.
- There are three other projects that are in early stages of development: (a) **Lubrajel Terra**, which is a plant-based "natural" Lubrajel product; (b) **Oil/Wax Hydration**, which is an anhydrous textured gel that can be added to the oil phase of a cosmetic formula, filling a need in the market for such a product (this is also being developed as a "natural" product); and (c) **Moisture-Lock Lubrajel**, which is being developed to increase skin moisturization beyond what can be done with current moisturizers. We have several prototypes of this product, which will undergo hydration testing during the winter months to determine which should undergo further development.

In regard to the impact of the coronavirus pandemic on the company's daily operations over the past few months, as a business considered "essential" in New York, we never ceased production, although when things were at their worst in New York we did modify our staffing in order to decrease employee density as much as possible. For a while, our employees worked 7 days a week on altered hours, and then went on an every-other-week work schedule with limited hours. As things improved, we gradually increased our working hours and employee density, and are now back on our regular working schedule. Early in the pandemic we had two employees that came down with the virus, but both recovered and returned to work. We also had two older employees terminate their employment with us due to their fear of contracting the virus. Since we are still concerned about exposing our employees to any interactions that are not absolutely necessary, we have not yet filled those positions. However, everyone at the company has been working together to fill the gaps left by these two departures, and we have been fortunate to be able to handle the additional workload without having to fill those positions yet. I am thankful to have the dedicated and hardworking employees that we have, who have enabled us to continue operating during this difficult time.

We will continue to do everything we can to increase the sales of our products as the world economies reopen, and intend to work closely with our marketing partners to expand the sales of our cosmetic ingredients as production of cosmetic products gradually resumes around the world. We are all looking forward to a time when a vaccine and/or treatment for the virus will be available so that we all get back to living our lives as we had before (or as close to that as we can get!). Until then, we will continue our commitment to developing new and innovative products for the cosmetic market, and are optimistic that we will continue to be profitable despite the difficulties that all of us are dealing with.

Sincerely,

UNITED-GUARDIAN, INC.



Ken Globus
President

Second Quarter 2020 **RESULTS FOR THE**
THREE AND SIX MONTHS ENDED
JUNE 30, 2020 AND JUNE 30, 2019

STATEMENTS OF INCOME

(UNAUDITED)

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	<u>2020</u>	<u>2019</u>	<u>2020</u>	<u>2019</u>
Net sales	\$ <u>2,954,644</u>	\$ <u>3,279,399</u>	\$ <u>6,277,558</u>	\$ <u>6,459,716</u>
Costs and expenses:				
Cost of sales	1,270,434	1,467,323	2,659,765	2,755,668
Operating expenses	511,635	502,094	1,026,910	1,049,056
Research and development expense	<u>108,566</u>	<u>93,846</u>	<u>216,298</u>	<u>192,504</u>
Total costs and expenses	<u>1,890,635</u>	<u>2,063,263</u>	<u>3,902,973</u>	<u>3,997,228</u>
Income from operations	<u>1,064,009</u>	<u>1,216,136</u>	<u>2,374,585</u>	<u>2,462,488</u>
Other income:				
Investment income	48,319	49,941	92,386	94,108
Net gain on marketable securities	<u>387,179</u>	<u>86,849</u>	<u>30,584</u>	<u>344,043</u>
Total other income	<u>435,498</u>	<u>136,790</u>	<u>122,970</u>	<u>438,151</u>
Income before provision for income taxes	1,499,507	1,352,926	2,497,555	2,900,639
Provision for income taxes	<u>312,896</u>	<u>274,116</u>	<u>520,637</u>	<u>599,135</u>
NET INCOME	\$ <u>1,186,611</u>	\$ <u>1,078,810</u>	\$ <u>1,976,918</u>	\$ <u>2,301,504</u>
Earnings per common share (basic and diluted)	\$ <u>0.26</u>	\$ <u>0.23</u>	\$ <u>0.43</u>	\$ <u>0.50</u>
Weighted average shares (basic and diluted)	<u>4,594,319</u>	<u>4,594,319</u>	<u>4,594,319</u>	<u>4,594,319</u>

BALANCE SHEETS*

(condensed)

	JUNE 30, <u>2020</u> (UNAUDITED)	DECEMBER 31, <u>2019</u> (AUDITED)
<u>ASSETS:</u>		
Current assets	\$ 12,112,642	\$ 11,567,281
Property, plant, and equipment	7,393,521	7,390,525
Less: Accumulated depreciation	<u>6,683,500</u>	<u>6,609,818</u>
Net property, plant and equipment	710,021	780,707
Other assets (net)	<u>7,412</u>	<u>14,824</u>
TOTAL ASSETS	\$ <u>12,830,075</u>	\$ <u>12,362,812</u>
<u>LIABILITIES AND STOCKHOLDERS'</u>		
<u>EQUITY:</u>		
Current liabilities	\$ 2,025,027	\$ 1,343,059
Deferred income taxes (net)	124,846	386,855
Stockholders' equity	<u>10,680,202</u>	<u>10,632,898</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ <u>12,830,075</u>	\$ <u>12,362,812</u>

* More detailed financial information can be found in the company's Form 10-Q for the second quarter of 2020, which can be found on the company's web site at www.u-g.com.