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UNITED GUARDIAN INC
Form 10KSB
March 28, 2007

U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-KSB

(Mark One)

ANNUAL REPORT UNDER SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934

For the fiscal year ended December 31, 2006.

OR

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 1-10526

UNITED-GUARDIAN, INC.

(Name of small business issuer in its charter)

Delaware

11-1719724

(State or other jurisdiction
of incorporation or organization)

(I.R.S. Employer Identification No.)

230 Marcus Blvd., Hauppauge, NY

11788

(Address of principal executive offices)

(Zip Code)

Issuer's telephone number, including area code: (631) 273-0900

Securities registered pursuant to Section 12(b) of the Exchange Act: None

Title of each class: Common Stock, \$.10 par value

Name of each exchange on which registered: American Stock Exchange

Check whether the issuer is not required to file reports pursuant to
Section 13 or 15(d) of the Exchange Act.

Check whether the issuer: (1) filed all reports required to be filed by
Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such
shorter period that the registrant was required to file such reports), and (2)
has been subject to such filing requirements for the past 90 days.

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Yes No

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Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.)

Yes No

The registrant's revenues for the fiscal year ended December 31, 2006 were \$12,195,672.

On March 1, 2007 the aggregate market value of the Registrant's Common Stock (based upon the closing sales price of such shares on the American Stock Exchange as reported in The Wall Street Journal) held by non-affiliates of the Registrant was approximately \$21,012,600 (Aggregate market value has been estimated solely for the purposes of this report. For the purpose of this report it has been assumed that all officers and Directors of the Registrant, as well as all stockholders holding 10% or more of Registrant's stock, are affiliates of the Registrant. The statements made herein shall not be construed as an admission for determining the affiliate status of any person.)

As of March 1, 2007 the registrant had issued 5,004,739 shares of Common Stock, \$.10 par value per share ("Common Stock"), of which 4,942,539 shares were outstanding and 62,200 shares were held as Treasury stock.

DOCUMENTS INCORPORATED BY REFERENCE:

Certain information required by Part III (portions of Item 9, as well as Items 10, 11, and 12) is incorporated by reference to the registrant's definitive proxy statement for the 2007 annual meeting of stockholders ("2007 Proxy Statement"), which, pursuant to Regulation 14A of the Securities Exchange Act of 1934, as amended, is to be filed with the Securities and Exchange Commission no later than 120 days after registrant's fiscal year end.

Transitional Small Business Disclosure Format (check one): Yes No

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This annual report on Form 10-KSB contains both historical and "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, which provides a safe harbor for forward-looking statements by the Registrant about its expectations or beliefs concerning future events, such as financial performance, business prospects, and similar matters. The Registrant desires to take advantage of such "safe harbor" provisions and is including this statement for that express purpose. Words such as "anticipates", "believes", "expects", "intends", "future", and similar expressions identify forward-looking statements. Any such "forward-looking" statements in this report reflect the Registrant's current views with respect to future events and financial performance, and are subject to a variety of factors that could cause Registrant's actual results or performance to differ materially from historical results or from the anticipated results or performance expressed or implied by such forward-looking statements. Because of such factors, there can be no assurance that the actual results or developments anticipated by the Registrant will be realized or, even if substantially realized, that they will have the anticipated results. The risks and uncertainties that may affect Registrant's business include, but are not limited to: economic conditions, governmental regulations, technological advances, pricing and competition, acceptance by the marketplace of new products, retention of key personnel, the sufficiency of financial resources to sustain and expand Registrant's operations, and other factors described in this report and in prior filings with the United States Securities and Exchange Commission ("S.E.C.") Readers should not place undue reliance on such forward-looking statements, which speak only as of the date hereof, and should be aware that except as may be otherwise legally required of Registrant, Registrant undertakes no obligation to publicly revise any such forward-looking statements to reflect events or circumstances that may arise after the date hereof.

PART I

Item 1. Description of Business

(a) General Development of Business

United-Guardian, Inc. ("United" or "Registrant") is a Delaware corporation that, through its Guardian Laboratories Division ("Guardian"), conducts research, product development, manufacturing and marketing of cosmetic ingredients, personal and health care products, pharmaceuticals, and specialty industrial products. United also distributes an extensive line of fine organic chemicals, research chemicals, test solutions, indicators, dyes and reagents through its wholly-owned subsidiary, Eastern Chemical Corporation ("Eastern"). Unless otherwise specified or indicated by the context, "Company" shall refer to United-Guardian, Inc. as well as its divisions and subsidiaries.

United's predecessor, United International Research Corp. (which name was later changed to United International Research, Inc. ("UIR")), was founded and incorporated in New York in 1942 by Dr. Alfred R. Globus, United's Chairman and Director of Research. On February 10, 1982, a merger took place between UIR and Guardian Chemical Corp. ("GCC"), an affiliate of UIR, whereby GCC was merged into UIR and the name was changed to United-Guardian, Inc., a New York Corporation. On September 14, 1987, United-Guardian, Inc. (New York) was merged with and into a newly-formed Delaware corporation by the same name, United-Guardian, Inc., for the purpose of changing the domicile of United.

The following is a description of the two business segments in which the Company operates:

(1) Guardian conducts research, product development, manufacturing and marketing of cosmetic ingredients, personal and health care products, pharmaceuticals, and specialty industrial products. The research and development department not only develops new products but also modifies and refines existing products, with the goal of expanding the potential markets for the Company's products. Many of the products manufactured by Guardian, particularly its LUBRAJEL(R) line of products, are marketed worldwide through a network of distributors, and are currently used by many of the major multinational personal care products companies.

Guardian presently has a broad range of products, some of which are currently marketed, some of which are marketable but are not currently marketed by the Company, and some of which are still in the developmental stage. Of the products being actively marketed, the two largest product lines are the LUBRAJEL line of cosmetic ingredients, which accounted for approximately 70% of the Company's sales in 2006, and its RENACIDIN(R) IRRIGATION, a pharmaceutical product that accounted for approximately 17% of the Company's sales in 2006. The Company actively seeks other companies as potential marketers for its products, particularly for those products that are not yet being actively marketed by the Company.

(2) Eastern is a distributor of fine organic chemicals, research chemicals, intermediates, reagents, indicators, dyes and stains. It has been in business for over 50 years, the last 35 or so as a subsidiary of the Company. It carries an extensive line of products which it sells throughout the United States as well as overseas. Eastern's products are primarily sold either to distributors for resale in smaller quantities or as intermediates and raw materials for further chemical processing. Sales quantities range from a few hundred grams to over a thousand kilos per shipment. Although Eastern carries out no chemical manufacturing, it does contract with several custom chemical manufacturers and also will package-to-order for those customers that require it.

Paragon Organic Chemicals, Inc. ("Paragon") is a wholly-owned subsidiary of United that functions as a purchasing arm for Eastern. It has no assets or sales of its own.

(b) Narrative Description of Business

Guardian Laboratories Division

Guardian conducts research, product development, manufacturing and marketing of many different cosmetic ingredients, personal and health care products, pharmaceuticals, and specialty industrial products, all of which are developed by Guardian, and many of which have unique properties. The products manufactured by Guardian are sold to end users through the Company's marketing partners, distributors, direct advertising, mailings, and trade exhibitions. Guardian's proprietary cosmetic ingredients are sold through marketing partners and distributors and are incorporated into products marketed by many of the major international cosmetic companies. Many of Guardian's products are marketed through collaborative agreements with larger companies. The pharmaceutical products are sold to end users primarily through drug wholesalers. These sales include indirect sales to the Veteran's Administration and other government agencies. There is also a small amount of direct sales to hospitals and pharmacies.

During 2006, Guardian's sales accounted for approximately 92% of Company's total product sales.

Guardian's products are sold under trademarks or trade names owned by the Company. The marks for the most important products, LUBRAJEL and RENACIDIN, are registered as trademarks in the United States Patent and Trademark Office. In 2006 sales from these two product lines accounted for approximately 94% of Guardian's sales, and 87% of the Company's sales.

PRINCIPAL PRODUCTS:

LUBRAJEL

LUBRAJEL is a line of nondrying water-based moisturizing and lubricating gels that have applications in the cosmetic industry primarily as a moisturizer and as a base for other cosmetic products, and in the medical field primarily as a lubricant. In the cosmetic industry it is used primarily as a stable gel for application around the eyes and on the face and as an ingredient in skin creams and moisturizers, makeup, body lotions, hair preparations, salves, and ointments. As a medical lubricant it has been used on catheters, prelubricated enema tips, and thermometers. The most important product in the LUBRAJEL line in 2006 once again was LUBRAJEL CG, the original form of LUBRAJEL; the second largest revenue producer in the Lubrajel line was LUBRAJEL MS.

LUBRAJEL RR and RC are special grades of LUBRAJEL that can withstand sterilization by gamma radiation, which is one of the methods of terminally sterilizing medical and hospital products. On April 11, 1995, the Company was granted a U.S. patent for this unique form of LUBRAJEL. In September 1994 the Company entered into a marketing agreement with Avail Medical (formerly Horizon Medical), a California company engaged in the development and manufacturing of products and services to the medical device and pharmaceutical industries. Avail has been actively marketing LUBRAJEL RC since January, 1996. LUBRAJEL RR, the original radiation resistant form of LUBRAJEL, is sold to medical device manufacturers primarily for use in lubricating urethral catheters.

LUBRAJEL PF is a preservative-free form of LUBRAJEL currently being marketed primarily by Societe D'Etudes Dermatologiques ("Sederma") under the tradename "Norgel". Sederma is the Company's distributor of LUBRAJEL in France and a major European cosmetic ingredient supplier. It is also distributed by some of the Company's other marketing partners under the name LUBRAJEL PF. Tests conducted by Sederma indicated that the product self-preserved, and aided in the preservation of other cosmetic ingredients with which it was formulated.

LUBRASIL(TM) and LUBRASIL DS are special types of LUBRAJEL in which silicone oil is incorporated into a LUBRAJEL base by microemulsification, while maintaining much of the clarity of regular LUBRAJEL. The products have a silky feel, and are water resistant while moisturizing the skin. (These sales are already included in the total Lubrajel sales figure mentioned previously). The newest products in the LUBRASIL line are the new LUBRASIL II products, which currently consist of LUBRASIL II DM and LUBRASIL II SB. Both products contain 20% silicone compared with 1% for the original LUBRASIL products.

The Company believes that its ability to increase sales of its LUBRAJEL products will depend on (a) the ability of its marketing partners, especially ISP Technologies Inc. ("ISP"), its largest marketing partner, to continue to bring the product to the attention of new customers, and (b) the Company's success in bringing to market new forms of LUBRAJEL that will enable the product to be used in new applications. Guardian is continuing to develop new varieties of LUBRAJEL for this purpose. In 2004 Guardian introduced a new LUBRAJEL under

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the name "LUBRAJEL II XD", and at the end of 2004 it introduced an extensive new

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line of LUBRAJEL products using a different preservative system, which the Company believes will attract new customers and retain existing customers that might require a different preservative system. In 2006 Guardian developed the two new LUBRASIL II products mentioned above, which have enhanced feel and additional lubricating and/or moisturizing properties. The LUBRASIL II DM was completed and was sampled to the Company's marketing partners in the third quarter of 2006, and the LUBRASIL II SB was completed in 2006 and is expected to be introduced into the market in the second quarter of 2007.

The Company believes that there is still significant potential to expand the sales of its LUBRAJEL line of products through both product modifications and by geographic expansion, especially in developing markets such as mainland China, India, and eastern Europe. In furtherance of that goal, in December, 2006 it entered into an agreement with a marketing consultant, who will be working with the Company to expand the Company's product line into areas not currently being serviced by the Company's existing distribution arrangements. That consultant will initially be concentrating on expanding the medical uses for the Guardian's products, which has been a growing area in recent years.

The Company believes that any potential sales increases in the LUBRAJEL line of products may be offset by sales of competitive products. Despite this competition, the Company believes that it will still be able to expand the market for its LUBRAJEL product line. The Company believes that LUBRAJEL'S reputation for quality and customer service, as well as future additions to the LUBRAJEL line, will enable it to continue to compete effectively in the marketplace.

PHARMACEUTICAL PRODUCTS

RENACIDIN is a urological prescription drug, approved in the U.S. only, which is used primarily to prevent the formation of and to dissolve calcifications in catheters implanted in the urinary bladder. It is marketed as a ready-to-use sterile solution under the name "RENACIDIN IRRIGATION". RENACIDIN IRRIGATION is also approved for use in dissolving certain types of kidney stones. In October, 1990, the United States Patent Office issued to the Company patent #4,962,208, which expires in October, 2007, covering the method of manufacturing RENACIDIN IRRIGATION. The Company does not expect the expiration of this patent to affect its sales of RENACIDIN IRRIGATION because the brand name, RENACIDIN, has a long history of use and has become synonymous with this product category.

CLORPACTIN(R) WCS-90 is a microbicidal product used primarily in urology and surgery as an antiseptic for treating a wide range of localized infections in the urinary bladder, the peritoneum, the abdominal cavity, the eye, ear, nose and throat, and sinuses. The product is a white powder that is mixed with water and used as a solution. It is a powerful disinfectant, fungicide, deodorizer, bleach, and detergent.

OTHER PRODUCTS:

KLENSOFT(TM) is a surfactant (a surface active agent, such as a soap or detergent, that can reduce the surface tension of a liquid and thus allow it to foam or penetrate solids or act as a wetting agent) that can be used in shampoos, shower gels, makeup removers, and other cosmetic formulations. The primary customer for KLENSOFT for many years has been in Taiwan, but over the past few years there have been new customers for the product in the United

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Kingdom, Australia, France and Korea.

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CONFETTI(TM)DERMAL DELIVERY FLAKES is a product line introduced in 2000 that incorporates various functional oil-soluble ingredients into colorful flakes that can be added to, and suspended in, various water-based products. The product color and ingredients can be customized to meet the needs of individual customers.

ORCHID COMPLEX(TM) is a successor product to Guardian's previous Oil of Orchids product and is a base for skin creams, lotions, cleansers, and other cosmetics. This product is an extract of fresh orchids, modified by extractants, stabilizers, and preservatives, and is characterized by its excellent lubricity, spreadability and light emolliency. Because of its alcohol solubility, it may also be used in fragrance products such as perfumes and toiletries. Its light emolliency lends use in shampoos, bath products and facial cleansers. It is also a superior emollient for sunscreens, vitamin creams, toners and skin serums. It is sold in two forms, water-soluble and oil-soluble.

UNITWIX(R) is a cosmetic additive used as a thickener for oils and oil-based liquids. It is a proprietary, unpatented product that does not require government approval to market.

LUBRASLIDE(TM) and a related product, B-122(TM), are powdered lubricants used in the manufacture of cosmetics such as pressed powders, eye liners, and rouges. They are used as binders for these products, increasing their drop strength and lowering the coefficient of friction and water-repellency.

RAZORIDE(TM) is a clear, hypo-allergenic, non-foaming, water-based shaving product that is surfactant- and soap-free and has excellent lubricity and moisturizing properties.

DESELEX(R) is a replacement for phosphates in detergents.

HYDRAJEL PL and HYDRAJEL VM are personal lubricants and moisturizers developed specifically for the feminine personal care market.

Of these "Other Products", Klensoft comprised under 5% of the Company's sales in FY-2006, and the rest of the products combined made up approximately 3% of the Company's sales in 2006.

Development Activities

Guardian's research and development department has developed a large number of products that can be used in many different industries, including the pharmaceutical, medical, cosmetic, health care, and specialty chemical industries. These products are in various stages of development, some being currently marketable and some being in the very early stages of development requiring a substantial amount of development work to bring them to market. Research is also being done on new uses for currently marketed products.

Prior to initiating research and development work on a product, market research is done to determine the marketability of the product, including the potential market size and most effective method of marketing the product. After that the research and development department will determine whether the product can be successfully developed, including (a) laboratory refinements and adjustments to suit the intended uses of the product; (b) stability studies to determine the effective shelf-life of the product and suitable storage and transportation conditions for the product; and (c) laboratory efficacy tests to determine the effectiveness of the product under different conditions.

If that initial development work is successful, further development work to bring the product to market will continue, including some or all of the following: (a) clinical studies needed to determine safety and effectiveness of drug or medical device products; (b) preparatory work for the filing of Investigational New Drug Applications or New Drug Applications; (c) scaling up from laboratory production batches to pilot batches to full scale production batches.

While there can be no assurance that any particular project will result in a new marketable product or a commercially successful product, the Company believes that a number of its development projects, including those discussed below, may have commercial potential if the Company's development efforts are successful.

Guardian's major research focus is the development of new and unique personal care ingredients. The following are some of the projects that Guardian is either working on intends to work on in the near future:

LUBRAJEL II: This product line is being developed to recapture some of the market share that the Company has lost over the years to some of its competitors and to enhance the properties of the existing LUBRAJEL formulations. The first product in this line, LUBRAJEL II XD, was developed to be a drop-in replacement for an existing competitive product, and is currently being actively marketed. The second product, the LUBRASIL II DM, was initially sampled to the marketplace in August, 2006, and the third product, LUBRASIL II SB, is still in testing and should begin sampling in mid-2007. The Company hopes to continue to expand this product line over the next few years, introducing new formulations that have enhanced properties over competitive products. This new line is intended to be a supplement to, not replacement for, the current line of Lubrajel products. Its composition also will enable it to be used in certain countries, such as Japan, more easily than the current Lubrajel formulations.

CLORONINE: Cloronine is a powerful disinfectant, germicide, and sanitizer for disinfecting medical and surgical instruments and equipment (particularly where autoclaves are not available), and for the purification of water supplies. The product had been developed many years ago and had been approved for certain uses in France and Canada, and is still being sold on a very limited basis in Canada. The Company has been working with Howard Industries ("Howard"), an Ohio-based company that is interested in finding new markets for CLORONINE as a disinfecting agent. Howard has been testing it for a very specific farming application, and the results have been promising. They are currently awaiting the formal results of those tests and, if positive, Howard intends to begin marketing the product for that use in the second half of 2007. However, in order to do so it will have to register the product with one or more governmental agencies, including the United States Environmental Protection Agency, which could possibly delay their marketing efforts. Howard is also looking at other possible uses for Cloronine, and the Company is working on developing additional disinfecting agents, including one based on chlorine dioxide, which the Company hopes will open up new marketing opportunities with Howard.

CLORONINE GEL: This is another form of Cloronine that is being evaluated by Howard. It is a gel form of Cloronine, which makes it more effective on vertical surfaces. It, too, would require regulatory approvals before being marketed.

SELF-PRESERVING POLYMERIC THICKENER: This product will be a self-preserving raw material for cosmetic use that will enable cosmetic formulators to formulate preservative-free cosmetic products. Initial development efforts have produced mixed results so far, and this product is still in a very early stage of

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development.

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SKIN SENSORIAL AGENTS: A line of products that will enhance the feel of skin care products. The new Lubrasil II products mentioned are two examples of the new types of products the Company is looking to develop in this area.

MICROEMULSIFIED ANTIMICROBIAL: This would be a new form of antimicrobial product for use in skin disinfection products. The product could be sold either as a raw material or as a finished product in a hand cleanser.

The Company expects its research and development costs for 2007 to be comparable to those of the last two fiscal years. Any additional increase in development and/or production costs will depend on whether capital investments are required in order to continue development work on, or to manufacture, any of the new products under development.

Trademarks and Patents

The Company strongly believes in protecting its intellectual property and intends whenever possible to make efforts to obtain patents in connection with its product development program. The Company currently holds many United States patents and trademarks relating to its products, and regularly has patent and trademark applications pending with respect to a number of its research and development products. Patents formerly held by the Company on certain products have expired. There can be no assurance that any patents held by the Company will be valid or otherwise of value to the Company or that any patent applied for will be granted. However, the Company believes that its proprietary manufacturing techniques and procedures with respect to certain products offer it some protection from duplication by competitors regardless of the patent status of the products.

The various trademarks and trade names owned or used by the Company in its business are of varying importance to the Company. The most significant products for which the Company has a registered trademark are LUBRAJEL and RENACIDIN.

Set forth below is a table listing certain information with respect to all unexpired U.S. patents held by the Company:

PATENT NAME	PATENT #	FILING DATE	ISSUE DATE
Method of Preparing Time-Stable Solutions of Non-Pyrogenic Magnesium Gluconocitrate ("Renacidin Irrigation")	4,962,208	9/1985	10/1990
Iodophor; Polyethylene Glycol Alkylaryl-sulfonate Iodine complex	4,873,354	4/1988	10/1989
Iodophor; biocide; reacting polyethylene glycol, alkylarylsulfonate and Iodine water-propylene glycol solvent refluxing	5,013,859	4/1988	5/1991
Thermal Resistant Microbial Agent ("Cloronine")	4,954,316	12/1988	9/1990
Use of Clorpactin for the Treatment of Animal Mastitis & the applicator used in that treatment (owned jointly by the Company and Diversey Ltd.)	4,983,634	12/1988	1/1991
Stable, Active Chlorine Containing Anti-microbial	5,128,342	10/1987	7/1992

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Compositions ("Cloronine")

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Stabilized Beta Carotene	5,023,355	6/1990	6/1991
Gamma Radiation Resistant Lubricating Gel	5,405,622	12/1993	4/1995
Delivery system for oil soluble actives in cosmetic/ personal care products	6,117,419	9/1996	9/2000
Microemulsion of silicone in a water-based gel that forms a clear, transparent, highly stable moisturizer and lubricant for cosmetic and medical use	6,348,199	1/1994	2/2002

The Company requires all employees and consultants who may receive proprietary information to agree in writing to keep such proprietary information confidential.

Eastern Chemical Corporation

Eastern is a wholly owned subsidiary of United. It distributes an extensive line of fine organic chemicals, research chemicals, test solutions, indicators, dyes and stains, and reagents. In 2006 and 2005 Eastern's sales accounted for approximately 8% and 9%, respectively, of the total product sales of the Company. The Company's business activities and marketing efforts over the past several years have focused increasingly on the Guardian division, which the Company believes has greater growth potential than Eastern. As a result, the Company has reduced the amount of inventory kept on hand by Eastern, which in turn has resulted in some decline in its sales. There also has been a general decrease in Eastern's business due to competition from new companies in this field. The Company has considered, and will continue to consider, the possibility of selling Eastern at such time as it determines that keeping the operation is no longer in the Company's best interests. The Company believes that if it were to sell Eastern, the loss of revenue from that subsidiary would not have a material impact on the Company's net income.

Marketing

Guardian markets its products through: (a) distributors; (b) advertising in medical and trade journals, by mailings to physicians and to the trade; and (c) exhibitions at appropriate medical meetings. The pharmaceutical products are sold in the United States primarily to drug wholesalers that distribute to drug stores for resale, and to hospitals, physicians, long-term care facilities, the Veteran's Administration, and other government agencies. The proprietary personal care and specialty chemical products are sold to distributors for resale and directly to manufacturers for use as ingredients or additives in the manufacture or compounding of their cosmetic, personal care, or industrial products.

Eastern's products are marketed through advertising in trade publications and direct mailings. They are sold to distributors and directly to users in a wide variety of applications. Eastern does not sell any unique products and is not dependent on any single customer or group of customers on a continuous basis.

Domestic Sales

In the United States, Guardian's cosmetic products are marketed exclusively by ISP in accordance with a marketing agreement entered into in 1996 and

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subsequently amended and expanded in 2000, 2002, and 2005 (see "Marketing Agreements" below). ISP also has certain rights to sell some of Guardian's other

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industrial and medical products. In 2006, ISP's purchases for distribution in the United States were estimated to be approximately \$1,032,000 compared with \$1,237,000 in 2005, a decrease of 16.6%. These sales accounted for approximately 8.5% of the Company's sales (NOTE: ISP's domestic sales figure is an estimate based on sales information provided to the Company by ISP. The Company has no way of independently determining which of ISP's purchases from the Company are intended for domestic sale and which are intended for foreign sale.) The Company believes that the decrease in ISP's domestic sales of the Company's products was the result of the discontinuation by some customers of products that contained the Company's raw materials. However, this decrease in ISP's domestic sales was offset by an increase in ISP's foreign sales of the Company's products.

The Company's domestic sales of pharmaceutical products are handled primarily through the major full-line drug wholesalers and account for approximately 19.0% of the Company's sales. The Company's other products, such as its industrial products, are sold directly to end-users and account for approximately 1.0% of sales.

Foreign Sales

In 2006 and 2005 the Company derived approximately 52.0% and 51.0%, respectively, of its sales from customers in foreign countries, primarily from sales of its cosmetic products in Europe and Asia. The Company currently has six distributors for its personal care products outside the United States, with ISP being the largest. ISP has global distribution rights with the exception of the following: S. Black Ltd. in the United Kingdom; Sederma in France; Luigi & Felice Castelli S.R.L. in Italy; S. Black GmbH in Switzerland; and C&M International in Korea.

The Company's foreign sales attributable to each of its foreign distributors and/or customers as a percentage of the Company's total sales were as follows: ISP: 26.8% (an estimate of ISP's purchases intended for sale outside the U.S., based on sales figures provided to the Company by ISP); Sederma: 10.1%; S. Black: 6.0%; C&M International: 2.9%; Harmac: 1.4%; and Castelli: 1.0%. The Company also has two foreign customers for its medical products that each account for less than 1.0% of the Company's total sales.

Marketing Agreements

In 1994 the Company entered into a marketing agreement with ISP whereby ISP would distribute Guardian's personal care products, as well as some medical and industrial products, in certain parts of Europe, Asia, Australia, and Africa. ISP manufactures and markets an extensive line of personal care, pharmaceutical, and industrial products on a global basis. In 1996 the parties entered into another agreement, extending those distribution rights to the United States, Canada, Mexico, Central and South America. In July 2000 the parties entered into an Exclusive Marketing Agreement (the "2000 Agreement"), which modified, extended, and consolidated the 1994 and 1996 agreements. The 2000 Agreement also gave the Company greater flexibility in appointing other marketing partners in areas where ISP was not active or had not been successful, gave ISP certain additional territories, and granted ISP exclusivity in the territories assigned to it as long as annual minimum purchase requirements were met.

In December 2002 the parties entered into a letter agreement that extended and modified the 2000 Agreement. This was further modified in December 2005 to extend ISP's marketing rights until December 2008, and to provide for automatic extensions until December, 2010 if specified minimum annual purchase levels were attained. It also specified guidelines and provisions for future price increases

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by the Company.

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The Company believes that in the event ISP were to cease marketing Guardian's products, alternative arrangements could be made to continue to supply product to the customers currently using the Guardian's products without any significant interruption of supply.

The Company has other marketing arrangements with marketing partners in the U.K., France, Switzerland, Korea, and Italy, but all of these other arrangements are operating under either verbal agreements or expired written agreements, and are subject to termination at any time by either party.

Raw Materials

The principal raw materials used by the Company consist of common industrial organic chemicals, laboratory reagents, and common inorganic chemicals. Most of these materials are available in ample supply from numerous sources. The Company has five major raw material vendors that account for 91.0% of the raw material purchases for Guardian and 78.0% of the raw material purchases of the Company.

Inventories; Returns and Allowances

The Company's business requires that it maintain moderate inventories of certain of its finished goods. Historically, returns and allowances have not been a significant factor in the Company's business.

Backlog

The Company currently does not have any significant backlog.

Competition

Guardian has many products or processes that are either unique in their field or have some unique characteristics, and therefore are not in direct competition with the products or processes of other pharmaceutical, personal care, chemical, or health care companies. However, the ph