



# 2005 ANNUAL REPORT

to the Stockholders of  
**UNITED-GUARDIAN, INC.**

April 17, 2006

Dear Stockholder,

Once again we had a very profitable year in fiscal 2005, with sales exceeding \$12 million for the first time, and net income after taxes reaching a new high of over \$2.6 million. This was an increase in revenue of 9%, and an increase in earnings of 6%. The revenue increase for the Guardian division was even higher, almost 12%, but that was offset by a 5% decline in revenues of the Eastern Chemical division. Along with our sales and earnings growth our financial strength also continued to grow, with working capital increasing by approximately \$314,000 and our current ratio at a very strong 8.3 to 1.

As a result of our excellent financial condition we were once again able to increase our regular dividend, this time from the \$.18 per share we paid in January, 2005 to the \$.22 per share that we paid this past January. We were also able to repeat in June, 2005 the \$.25 per share special dividend that we paid in October, 2004, bringing the total dividend payments in 2005 to \$.47 per share, an increase of 9% over the \$.43 per share that we paid in 2004.

We believe that our dividend payments have been one of the factors causing the increase in our stock price over the past few years. We also have noticed increased interest on the part of money fund managers over the past year. Many of them have indicated that our strong financials and our cost conscious, conservative management style have brought our company to their attention. Despite the urging we have received from some of our investors to grow the company faster by making an acquisition, many other investors (and potential investors) have complemented us on having resisted that temptation until the right opportunity comes along. They have also praised our willingness to return some of our profits to our shareholders as long as we retain a sufficient percentage of those profits in case an acquisition opportunity does arise, which we have done.

During this past year we have focused our efforts on evaluating the personal care market to determine the most effective way to allocate our R&D resources. To further this goal we retained an excellent marketing consultant with whom we are working to help us prioritize our R&D work. The first stage of that work has been completed with the submission of a report that has given us some insight as to what might be the most productive avenues to explore. Over the next few months we will be discussing a continuing role for that consultant to assist us in bringing some new products to market, including new products for the medical (but not drug) market. The idea would be for her to assist us in marketing some existing products that are not currently being sold, either because they are finished formulas or because their primary uses are in other industries not covered by our current marketing partners, as well as to work with us to develop new products.

One of the first products to come from this input from our new consultant is a new form of Lubrasil™, our patented microemulsion of silicone in Lubrajel®, our water-based moisturizing gel. The new product will be marketed under the tradename "Lubrasil II Extra". This new product will have significantly higher levels of silicone. The existing product has silicone levels of about 1%, but we were finding that at that level many customers could not take advantage of the product. As a result, our goal for the new product is to incorporate 20% silicone, and we believe that we have succeeded. Although there still is work to be done on this product before it is ready to market, we plan to discuss its introduction with our marketing partners at the In-Cosmetics meeting in Europe this month, with the expectation that sales will begin in the third quarter of this year. We believe that the development of this enhanced product will open up a whole new market for this product.

Even though our Lubrajel product line has now been marketed for over 20 years, sales of the core products in that line continue to grow. In fact, most of the increase in sales we experienced this past year was attributable to increases in sales of Lubrajel "CG" and "MS", which are the original two products in that line. Most of the increase was due to the strong marketing effort being made by our largest marketing partner, International Specialty Products (ISP). ISP has been very successful in expanding our sales into growing markets like mainland China, and we expect to continue to work closely with them to continue this growth. In fact, we just signed a new agreement that extends our marketing agreement with them through at least the end of 2008, with the possibility of an additional automatic extension through 2010 if certain annual sales increases are

achieved. We also are confident that our other marketing partners will also be able to increase their sales as we provide them with new products as well.

For those who missed our Interim Letter, we were very pleased to learn that Gillette has incorporated our Lubrajel Oil in their new line of "Fusion" shaving gels, which are accompanying the introduction of their new Fusion razor. They have also incorporated another form of Lubrajel in one of the Fusion after-shave products. Although the amount of our product in each can is relatively small, Gillette is expected to be heavily promoting this product line, and we are very excited to be part of it. We hope this will be just the first of many products that we can work on with Gillette.

Sales of our new Lubrajel "Free" line of paraben-free products have also grown this past year, and we expect this growth to continue as more companies choose to bring out paraben-free products. Sales of Lubrajel for medical uses, such as catheter lubrication, also grew significantly this year, and we intend to put more resources this year into this market, which we believe has excellent potential for increased sales.

There are certain new projects that I cannot discuss because we have not yet filed for patent protection, but here is a description of some of the projects that I can mention:

- ❖ A new polymer-based thickener that will have some exciting and unusual properties. We are in the process of preparing disclosures for a future patent filing, so I cannot expand upon this any further until that is done. This is still in an early developmental stage.
- ❖ Skin sensorial agents: This area of research was brought to us by our new consultant. It will involve developing new products that will enhance the feel of skin care products. We already have some ideas for products, but the work is in its preliminary stages. Our Lubrasil II Extra will be one of the first products in this category to be marketed.
- ❖ Enhanced antimicrobial product: These efforts will be focused on improving a popular antimicrobial ingredient currently used in hand washes and other antimicrobial products. Our goal is to develop a new version of the product that will have better compatibility with various raw materials.
- ❖ New products for the "LUBRAJEL II" line: we currently have one product in this line, the Lubrajel II "XD". The new enhanced Lubrasil II Extra mentioned above will be the second product. The purpose of this line was to bring out new Lubrajel products with enhanced properties, and we hope to add additional products in the coming years.
- ❖ Cloronine™: We are currently working with a company that has managed to get Cloronine, our chlorine-based disinfectant, into a government testing program designed to find new antimicrobial products for decontamination. It is taking longer than we expected to begin the testing, but we have recently been informed that testing should begin in September. We have also developed a gel form of that product which may be even more effective for vertical surface decontamination.

It has been a very productive and profitable year for us, and we are very excited about the work we are doing on some of these new products. With the help of our new consultant and our marketing partners we are confident that we will be able to continue to bring innovative products to the marketplace. While we are always open to the possibility of an acquisition if the right opportunity presented itself, for now we will continue to do the things we are good at, which is increasing our internal R&D efforts to develop innovative and unique personal care products. We have supplemented our R&D staff this year to enable us to expand those efforts.

Our goal is to continue to strengthen our financial position, with the expectation of continuing to share our success with our shareholders through the issuance of regular (and possibly special) dividends. We are very pleased with the confidence our stockholders have shown in us (as evidenced by the strong stock price), and we hope that all of our stockholders will continue to support us as we continue our steady growth through the introduction of innovative new products into the personal care market.

Sincerely,

UNITED-GUARDIAN, INC.



ALFRED R. GLOBUS  
Chairman and C.E.O.