

SECOND QUARTER 2024 CONFERENCE CALL

Jess Jankowski, President & CEO

Thank you, Shannon. Good morning to all of those listening live and thank you to those following up later online.

Well, we're rolling. We had a strong Q2, following a strong Q1, and we've got our foot on the gas working to make 2024 a record year for Nanophase and Solésence. Kevin Cureton, our Chief Operating Officer, is joining me again on the call today. We have some prepared comments, then we'll be available for some Q&A afterward.

Q2 of 2024 saw us with quarterly revenue of \$13 million dollars. For the first half of 2024, we had almost \$23M in revenue. To put this in perspective, \$23M in revenue for the 1st six months of 2024 is 33% more than our \$17M in FULL YEAR 2020 revenue, which was a major milestone at that time.

We believe that second half revenue will exceed the 1st half, with the potential for us to achieve more than \$50M in revenue for the year. With upside, we can do better than that.

Before I walk you through the numbers, I'm going to spend a minute describing our business at a high level. We've had several investors asking questions about this, and I want to be sure that we bring clarity to the story. The better we understand it, the more exciting our progress is.

Nanophase, and its wholly owned subsidiary Solésence, are almost two sides of the same coin. Nanophase is an FDA-regulated manufacturer of bulk pharmaceutical ingredients. These active ingredients serve as the backbone for everything both companies do. We started with an active ingredients business in Nanophase, providing the safe and effective UVA and UVB protection found in minerals-based sunscreens, through BASF. This market grew significantly in the late teens and into the early twenties. There was a limiting factor in the growth of minerals-based sunscreens, however, and that was the whitening effect of most zinc oxide additives. Our initial claim to fame was that our coated zinc oxide active ingredient, which we exclusively supply to the market through BASF, was superior to other minerals-based ingredients. This continues to be a good market for us, as BASF continues to be a good partner in that market.

In 2016-17, we realized that we needed to take a new approach to capitalize on the growing demand for minerals, particularly for zinc oxide, in the market for daily wear and functional cosmetics. Dr. Harry Sarkas, along with a cast of talented scientists, was able to take our particle performance beyond the next level. We developed the Solésence technology to allow larger zinc oxide particles, referred to as "non-nano" in the industry, to be incorporated into various lotions without exhibiting what is referred to as "ghosting" in the market. We then built a formulating team with solid industry experience to help us to show cosmetics companies, which we refer to as "Brands," to see the benefits of Solésence technology. By enabling very uniform and flexible particles, then a series of methods by which to disperse and formulate with them, we were able to create finished prestige cosmetics products, which had the functionality of sunscreens, built into everyday cosmetics. We'd found the "holy grail" in a respect. People getting ready for their day would be able to know they were getting protected against

UVA, UVB, and other skin damage, which everybody wants, but by a product that otherwise seemed just like the high-end cosmetics they would typically use anyway.

Coupling this massive advancement with the consumer trend against chemicals-based UV protection, along with the FDA's repeated assertions that minerals are proven safe for use, whereas chemicals-based absorbers lack such public proof, we hit this market at an excellent time.

We took our FDA-compliant practices, which presented a barrier to entry for many potential competitors, and were unfamiliar to many of our Solésence customers, and coupled it with 25+ years of experience making safe, minerals-based active ingredients. We created a value proposition that is only just starting to show its true potential.

Solésence sells through "Brands," not direct-to-consumers. This means you'll rarely see mention of Solésence in Brand advertising, or on packaging, but we are the enabling feature of the products our Brand partners sell.

That was a quick summary I know, but we wanted to take a few minutes to ground our new investors, potential investors in why we've been so successful, and as a refresher for everyone else.

OK. Now, let's walk through the numbers. Unless identified otherwise, all numbers will be stated in approximate terms.

We had a strong 2nd quarter, with \$13M in revenue, a 32% increase over 1st quarter revenue, and a 10% increase over the 2nd quarter of 2023. We had a 29% gross margin, including a write-down of our component inventory of approximately \$500K, reducing our Q224 gross margin by about 4%.

For the six-month period, we had \$22.9M in revenue with a 32% gross margin. I want to spend a minute discussing our inventory, which you may have noticed is up \$3.8M since year-end. We intentionally bulked-up our inventory to ensure that we could support all of the growth we're seeing now.

I want to explain the write-down, and how we addressed the circumstances that created it. The write-down was related to components, (think bottles, tubes, cartons, and labels), that became obsolete in Q2. Most related to two customers. Given our past struggles with supply, and the 3 – 6-month lead times on component supply, we decided to lean forward and order extra components in 2023, without having a guarantee that they would be used. We were focused on strengthening our supply chain by ensuring supply, which you may recall was a major issue at that time. For Q2, the customer's demand changed, and product specs came into question, resulting in obsolescence without an opportunity for us to claw anything back. We acquired these components in 2023, prior to implementing many of the changes we are seeing operate so effectively during 2024, which I'll now review.

To protect ourselves from production shortfalls, we've done several forward-focused things, that we believe will mitigate the demand issues we were plagued with much of last year, and certainly during 2022. We increased our staffing in our Supply Chain area, we are performing regular cycle counts of all of our inventory, and we review weekly KPIs with targets for raw materials requirements at 4 weeks and 12 weeks out. We hover between 98% and 100% on these metrics, giving us a much more comfortable margin of safety as we approach actual production dates. We have also added a full-time, dedicated scheduling professional with industry experience. This will allow our operating people to better focus on maximizing efficiencies and dealing with issues on the plant floor more immediately.

Having such focus and familiarity with our inventory has resulted in a raised awareness of what our risks are, and how to control them.

On the other side of the equation, we have adopted a uniform approach in the way we work with our customers, in terms of sharing responsibility for financing raw materials inventory, and managing market risk. Between our supply chain and sales teams, we have implemented policies that we believe have achieved a good balance, between having enough inventory on-hand to meet demand, not having to finance 100% of it in advance, and avoiding unnecessary cost exposure through the accumulation of inventory without supporting purchase orders, or customer deposits, or often both.

Without this \$500K reserve, there would've been a 4% and 2% increase in Q224 and 1st half 2024 margins, respectively, bringing our gross margins up to approximately 33% and 34% for the same respective periods.

This was a long way of explaining that we don't believe this type of write-down is something to expect going forward.

In addition to our supply chain improvements, we also expect gross margins to improve, through the combination of additional order volume, better management of smaller production runs, and the addition of new capacity, as we go through 2024.

We also expect second half '24 volumes to be at least 20% stronger than the first half.

Operating expenses year-over-year were down about \$1M. The bulk of the savings in SG&A was due to the BASF litigation costs tapering off as we settled our lawsuit with BASF in Q1. We remain focused here and expect to continue to control expenses. We're also seeing the benefits of our Q42023 restructuring as operating expenses have not grown in light of our incredible growth in 2024.

The bottom line showed excellent progress, with Q224 net income of \$900K, a \$500K+ improvement over Q2 of 2023, even with the \$500K write-down we just discussed.

For the six-months ended June 30th, 2024, we had \$1.7M in net income, compared to an \$800K net loss for the same period in 2023, a two-and-half-million-dollar swing.

In a few minutes, Kevin's going to address our operating performance. Many of our KPIs will be enhanced further through our investments in additional equipment and, at least as importantly, additional experienced technicians to keep them running smoothly.

As we have had the opportunity to augment our production staff, we have benefitted from bringing in more people with significant industry experience. This has created not just the benefit of having more experienced hands doing the work, but also the advancement of knowledge among our loyal, hard-working, and talented internally developed team members. We expect both our units produced, and revenue generated per employee, to continue to improve through these efforts.

We did a bit of a deep dive into capital projects last time, so today we'll just leave it at a high level. We intend to fund any required capital through operations in 2024, with our initial projects focused on bringing our potential capacity up to about \$100M in Solésence finished products. Total capital expenditures for this year should be in the \$3M - \$6M range, some of which may well slip into 2025.

Operationally, we're focused on improving our labor per unit, while also ensuring that our throughput can meet expected demand, through targeted capital improvements. We have some opportunities in our current pipeline that could generate significant growth in 2025. This is in addition to the expanded demand we're expecting to continue, from some of our existing Solésence customers.

Now I'd like to invite Kevin Cureton, our Chief Operating Officer, to share his thoughts on our progress so far, and the approach we're taking going forward. Kevin?

Kevin Cureton, Chief Operating Officer

Thanks Jess,

As usual, I would like to begin by thanking our teammates who every day demonstrate that we are indeed best in the industry at what we do, and our investors who continue to trust our leadership as we prove that through enhancing lives through healthy skin we can profitably grow at more than 3 times the growth rate of our industry. I also would like to thank the families of our teammates for their energy and support as we take this journey together.

During the Q1 conference call, we promised to not only review the operating KPIs we have discussed in the prior calls but to also introduce and discuss our growth KPIs. So let's jump right into it.

First the operating KPIs. Starting with Inventory Availability – which our purchasing team considers the on-time in-full or OTIF metric for the materials and components we buy. We have improved on our performance from last quarter as this metric is now 100% of our target performance – which is to have greater than 95% availability for materials due in twelve weeks and 98% availability for materials due in 4 weeks. This is both an excellent and vitally important result as without this outstanding performance, we wouldn't be able to achieve our other two operating KPIs. Our purchasing team has also made good progress on implementing our vendor development and management programs which includes amongst other elements bringing in additional qualified sources from around the world for key materials to minimize our out-of-stock risks and reliance on single source suppliers were possible. Their work gives us a high level of confidence in our ability to support even greater volume growth with minimal risk of supply shortages.

Our second operating KPI, Throughput, remained essentially unchanged from Q1 at 72% of target, however this was done on an overall volume increase of 158% over Q1. This improvement in total units produced - achieved by our manufacturing and supply chain teams - is what enabled us to achieve the record performance for Solésence. In Q3, we will need to achieve a similar 150% improvement in Throughput to meet what is record levels of demand for our products – which is largely a result of substantial increases in both domestic and European sell through for our largest brand partner Colorescience and over a dozen successful new launches with new brand partners such as Tatcha.

Our final operating KPI, OTIF remained below target at less than 50% of our goal. As you will hear when we discuss our growth KPI's, our growth in Q2 significantly outstripped our improvements in output, which has meant that we made tough production decisions – such as operating at suboptimal production runs to ensure our brand partners have the product quantities they need for a successful new launch. To put even greater focus on improving OTIF, our company is implementing Overall Equipment Effectiveness or OEE methodologies to target the specific changes needed to improve our operating uptime and therefore Throughout. Our work in this area only began a little more than 60 days ago, and we are already achieving small wins as we have made solid progress in increasing up time. This improvement resulted in our company achieving the best revenue month in our history during July.

Let's now spend a little time on our growth KPIs, Order Velocity, customer acquisition cost, and Pipeline Value. Order velocity measures the rate that we are generating new sales orders for our business. While we measure this weekly, it is particularly informative when we look at the year-to-date Order velocity versus plan. On a year-to-date basis, our order velocity is running at 125% of plan – an excellent result. Kudos to our business development and our product development teams for their outstanding work in this area. Similarly, the BD, PD and marketing teams are driving improvements in Pipeline Value – which measures the total value of new business opportunities that we expect to convert to revenue and our Customer Acquisition Costs or CAC which measures how much it costs us to acquire the new business. While our Pipeline value is not yet meeting our very lofty goal which is essentially to double 2024 revenue, we are at over 60% of target – still a very respectable result given the more than 40% year over year growth we will achieve in 2024. Further, we are doing this while lowering our customer acquisition cost by over 30%. While this is a solid performance, it also suggests that it's time for us to consider even greater investments in the departments that drive revenue growth. We've already started this work with programs underway to expand both the staffing and capabilities of our product development and quality teams.

In closing, as I mentioned in the press release, our company, through the close collaborations we have with our brand and supplier partners, is redefining what it means to have healthy, beautiful skin. This work is possible because of all the fabulous teams within our company. We have talked again and again about handling hard better – and they answered the call - we then asked them to raise their

expectations for what great looks like and they are achieving this too. We have and will continue to push our teams hard – but every time every team from finance to quality and everyone in between – rings the bell. While our technology and know how is second to none - it's our people that ultimately make the difference and will be reason that we continue to outperform our market in terms of growth and profitability.

Back to you Jess.

Jess Jankowski, President & CEO

Thanks, Kevin.

We have more than \$50M in shipped and confirmed sales orders through this week, and we expect more to follow.

As many of you know, we have not had problems generating customer demand. The markets like our Solésence products, and they want more. Our biggest challenge has been to meet that demand. It's been a limiting factor for several years. While we're not through yet, we have been successful in addressing that limiting factor this year, and we expect the 2nd half to show more evidence of that, in addition to more growth.

While we know that most of our investors listen to the webcast, or review the transcript, after the live call, we're happy to invite those of you participating live on today's call to ask any questions you may have, or to share your feedback. Afterward, I'll offer a few closing comments.

Shannon, would you please begin the Q&A session?

11:30 AM

Q&A SESSION PLACEHOLDER

12:00 PM

Thank you, Shannon. And thanks to all of our investors for hanging in there as we turn the corner. We're now seeing the results of executing on the strategy that we outlined several years ago. We have become the exciting company we'd all hoped for. We knew it would happen, but the "when" was elusive. We're just beginning at this point and our future is bright.

I hope everyone can finish their day with a smile, when you think about Solésence, and Nanophase, and the potential yet to be realized.

Thanks for being with us today.