

ASX ANNOUNCEMENT

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Improved operating result in COVID-impeded transition year

- **32% reduction in net operating loss in FY20**
- **Transition year to pure own-IP technology focus with 90% + gross margins**
- **Solid new business progress despite COVID impediments**
- **Excellent advances across technology suite**

Product authentication and consumer engagement solutions provider **YPB Group Limited (ASX:YPB)** presents highlights of preliminary financial results for the year ended 31 December 2020.

YPB recorded a clearly improved operating financial result in FY2020 with net operating loss reducing 32% from \$5.5m in FY2019 to \$3.7m in FY2020

Three prime determinants shaped the result:

- A 45% or \$0.5m fall in revenues. This was primarily the closure of the Retail Anti-Theft (RAT) business during 2019 with part-period revenues in that year not repeated in 2020. Foregoing this revenue was a conscious choice to streamline and solely focus the business on high margin, in-house technologies;
- COVID-19 disruption of normal customer order flows and hindrance of new business development; and
- A 33% or \$2.1m fall in operating costs from continuous business improvement but supported by temporary COVID-19 emergency salary reductions in Q2 2020 and zero Directors' fees from April to year end.

The major moves in costs were:

- A reduction in numerous consulting fees of \$1m;
- Employees costs down \$0.335m;
- And significant reductions in production costs (no RAT), rental (greater virtual office use), marketing (fewer promotional events) and travel.

The benefit of the change in operating focus to solely in-house intellectual property products was evident in gross margin rising from 82.8% in FY2019 to 93.7% in FY2020. Such high margins are key to the company's drive to profitability with each incremental revenue dollar falling almost entirely to the bottom line.

The improved trends in the accrual accounting results discussed above are confirmed by operating cashflows which saw 27% less operating cash consumed by the company in FY2020 over the prior year with:

- Cash receipts down 64% or \$1m in FY2020 on pcp but more than offset by;
- Cash payments falling 35% or \$2.1m in FY2020 on pcp.

In contrast to the above trends of clear improvement in operating results, the *statutory* result saw a 34% deterioration to a \$10.7m net loss. This was due to *non-cash* accounting adjustments to reflect “fair value losses” from issuing equity to extinguish financial liabilities. These liabilities included the settlement of a short-term loan from YPB's Executive Chairman, compensation for two years of cash-saving salary sacrifice by YPB's Chief Financial Officer, and an advisory group being willing to take YPB equity to assist the company with cash conservation.

The fair value losses arose due to a rise in YPB's share price between the time the company and the parties definitively agreed terms, including the price at which new equity would be issued, and the time the shares were issued. The share price at the time of issue was higher than the agreed price and the accounting standards require that the difference be taken through the profit and loss account. The standard effectively argues that the company transferred more value than the liabilities that were extinguished but the reality is had the share price been stable there would have been minor fair value loss. Nevertheless, the actual outcome was that the liabilities were eliminated, YPB retained cash and key parties demonstrated positive conviction as to the company's prospects by taking payment in equity.

Of these liabilities, the dominant one was to the Executive Chairman and, consequently, it accounted for the bulk of the fair value loss and bears further explanation. Still being in an investment phase, YPB is periodically dependent on external capital to fund operations. In Q1 and Q2 of 2020 as the dawning of the COVID pandemic roiled financial markets, the prospect of Australian micro and nano-cap companies raising funds was close to zero. In February 2020 as global equity markets were in freefall, the company needed new funds to remain solvent. After exhaustive endeavours and on the advice of the company's capital markets advisor, the Independent Directors agreed to a \$600,000 six-month loan at 8% p.a. from the Executive Chairman as the only possible source of funding for the company. A condition of the loan was convertibility to equity with attaching options. The price agreed was at a typical discount to the then share price as per normal market practice. The exercise price for the options was at a 100% premium to the share issue price. This issue of shares and options was approved by shareholders at the Annual General Meeting in July 2020.

The Executive Chairman loaned a further \$600,000 to the company in May 2020 on the loan terms but with no conversion rights. This second loan was repaid by the company in November 2020.

In short, the Executive Chairman twice provided critical emergency funding to the company, half of which was repaid in cash and half of which was left in the company via rolling the loan into equity. The ‘fair value loss’ was required by accounting standards but academic. The practical reality was a better funded company with additional permanent capital issued at a price which was fair at the time the funding was provided. The accounting loss only arose due to the size of the discount between the issue price and the market price at the time of issue.

Solid commercial advances in 2020 strengthen the platform for future business development

Over 2020, both the flow of customer orders and new business development were disrupted by COVID-19.

Signing new customers in 2020 slowed due to COVID-19 with companies cutting costs and almost no opportunity for live product demonstrations, a critical element of deal closures.

Despite this, our commercial teams strengthened existing and secured new channel partners, YPB's leveraged conduits to end customers. Numerous targeted joint business development programmes and product innovation ideas were created and advanced. These activities laid valuable foundations from which to drive new business wins in 2021, COVID-19 restrictions permitting.

YPB China produced the best sales result in its history with revenues up 28%, albeit well short of internal targets as COVID-19 restrictions in China were more persistent than understood ex-China. Nevertheless, a range of channel partners and new end-customers were developed during the year. Just as importantly, the strategy of more methodical account management of existing clients proved successful with the repeat business and recurring revenues base in China solidifying considerably.

In Australia, existing customers and order flows slowed with COVID-19 impacts, particularly those with exposure to the travel-ban ravaged Daigou trade. But important new customers such as Nature One Dairy and Nature's Care were added during the year and valuable new channel partner relationships were advanced.

The forthcoming Annual Report will review the company's commercial activities of 2020 in more detail.

2020's major technical advances set up for greater commercial success in 2021

i. MotifMicro – world first forensic product authentication by smartphone

MotifMicro is the company's revolutionary mass-market product authentication solution with enormous commercial potential. Major technical milestones toward commercial launch in H1 2021 were passed during the year with high accuracy recognition of the novel MM1 forensic authentication particles by both iOS and Android smartphones under 'real world' conditions.

Further, with each smartphone model having its own camera quirks the software app must be fine-tuned to reliably identify the presence of MM1. During the year YPB's in-house Artificial Intelligence lab expanded MotifMicro's capability to a portfolio of the most popular iOS and Android smartphones. This was an important step in maximising MotifMicro's practical commercial appeal and the project was largely complete by year end.

The other significant project during the year was enhancing the MM app to ensure a good user experience and maximise scan success rates. Significant progress was made and this project is slated for completion in late Q1 or early Q2.

ii. Connect – product authentication and consumer engagement SaaS platform

During 2020, the Connect 2.0 Customer Engagement SaaS platform was completed to commercial readiness. All clients were successfully migrated to the new platform by year end.

Connect 2.0 has been well received by YPB's customers, particularly its self-serve consumer data analytics capabilities. In fact, numerous requests for further product enhancements have been enacted and the product development roadmap is being strongly customer led.



A complete re-architecting of Connect 2.0 now sees it with greatly increased scalability and efficiency of resource use compared with its predecessor. Increased volumes from current and new customers can be accommodated quickly and efficiently and at negligible incremental cost. Further, Connect 2.0 now only uses hosting resources 'on demand' and is much lower cost to operate compared with an 'always on' service.

In summary, the technical progress with YPB's product authentication solutions, consumer engagement platform and the integration between the two solution sets during 2020 was very significant. The product suite has great commercial relevance and flexibility in tailoring technologies to solve each client's specific problems.

Outlook

2020 laid solid foundations for accelerated commercial progress and improved financial outcomes in 2021.

Channel partner and end-customer relationships were significantly advanced and clear routes to market with powerful partners see us well placed to drive new business.

Our technical progress has created a product suite able to solve counterfeit and marketing problems for brands with low cost, effective product authentication and consumer engagement solutions. Our flagship, revolutionary product authentication solution MotifMicro will be in-market with its first client in H1 2021 and there are early indications that other opportunities might slipstream in its wake.

Costs are contained and tightly controlled, and will remain so.

Together these factors support genuine optimism as to further significant improvement in financial results in 2021. That positivity, however, must be tempered by the reality that COVID-19 obstacles are still frustrating business development and order flows, and it is unclear when normality will resume.

Overall, the present business plan is for further significant financial improvement subject to unforecastable COVID-19 impacts.

YPB Group CEO John Houston said: *"I'm pleased with our improved financial result for 2020 despite the many handicaps of COVID-19 and the fact that 2020 revenues suffered in completing the transition to a sole focus business with much larger, less competitive, more profitable opportunities.*

The bitter disappointment of the year was having to issue equity at extraordinarily low prices and the subsequent dilution of shareholders but this poor outcome was unavoidable and superior to the imponderable alternative.

Despite these difficulties I am proud of the effort and outcomes that our team produced.

Our technical progress was unequivocally terrific and both customers and prospects recognise that we now have market leading, elegant solutions that protect against counterfeit and transform product packaging into digital marketing assets at very low cost.

Our commercial progress was hamstrung by COVID-19 but our effort was unrelenting and real advances likely to bear fruit in 2021 were made.

While 2020 improved financially, I am far from satisfied with the outcome and the whole company is driving toward YPB being a profitable, self-funding, growth stock. We've made real strides in an obstacle-strewn year and intend to kick major goals in 2021.

This announcement has been authorised by the Board of YPB Group Limited.

Ends.



For further information please contact:

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About YPB Group

YPB Group Limited (ASX:YPB) is an Australia-based product authentication and consumer engagement solutions provider. YPB's proprietary smartphone enabled technology suite allows consumers to confirm product authenticity and, for brands, that triggers consumers' engagement.

The combination of YPB's smartphone authentication solutions and its SaaS Connect platform, creates 'smart' product packaging, opening cost-effective, digital and direct marketing channels between brands and their consumers. Connect gathers actionable data on consumer preferences. It can then host tailored marketing campaigns directly back to the scanning smartphone.

YPB is currently focused on the rapidly growing Australian, South East Asian, and Chinese markets. Its focus is dairy, cannabis, alcohol and cosmetics where the viral growth of fake products, particularly in Asia, affects brand value and endangers consumers. To learn more please visit: ypbsystems.com