
U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Quarterly Period Ended **March 31, 2021**

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Transition Period From _____ to _____

Commission file number **000-25727**

IKONICS CORPORATION

(Exact name of registrant as specified in its charter)

Minnesota
(State or other jurisdiction of
incorporation or organization)

41-0730027
(I.R.S. employer
identification no.)

4832 Grand Avenue
Duluth, Minnesota
(Address of principal executive offices)

55807
(Zip code)

(218) 628-2217

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class | Trading Symbol(s) | Name of each exchange on which registered |
|---|-------------------|---|
| Common Stock, par value \$.10 per share | IKNX | Nasdaq Capital Market LLC |

Indicate by check mark whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 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. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files.) Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer
Non-accelerated filer

Accelerated filer
Smaller reporting company
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: Common Stock, \$.10 par value - 1,977,854 shares outstanding as of May 7, 2021.

IKONICS CORPORATION
QUARTERLY REPORT ON FORM 10-Q

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PART I - FINANCIAL INFORMATION**ITEM 1. Condensed Financial Statements****IKONICS CORPORATION
CONDENSED BALANCE SHEETS**

| | March 31, 2021 | December 31, 2020 |
|--|---------------------------|------------------------------|
| | (unaudited) | |
| ASSETS | | |
| CURRENT ASSETS: | | |
| Cash | \$ 4,428,269 | \$ 3,693,845 |
| Trade receivables, less allowance of \$54,000 in 2021 and \$55,000 in 2020 | 1,545,527 | 2,119,213 |
| Inventories | 1,961,916 | 1,644,975 |
| Prepaid expenses and other assets | 210,895 | 125,969 |
| Income taxes receivable | 17,749 | 219,451 |
| Total current assets | <u>8,164,356</u> | <u>7,803,453</u> |
| PROPERTY, PLANT, AND EQUIPMENT, at cost: | | |
| Land and building | 9,556,586 | 9,556,586 |
| Machinery and equipment | 5,263,586 | 5,263,586 |
| Office equipment | 1,417,219 | 1,417,219 |
| Vehicles | 245,674 | 245,674 |
| | <u>16,483,065</u> | <u>16,483,065</u> |
| Less accumulated depreciation | (9,255,263) | (9,094,702) |
| Total property, plant and equipment at cost, net | <u>7,227,802</u> | <u>7,388,363</u> |
| INTANGIBLE ASSETS, less accumulated amortization of \$198,539 in 2021 and \$207,399 in 2020 | 243,819 | 243,583 |
| Total assets | <u>\$ 15,635,977</u> | <u>\$ 15,435,399</u> |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| CURRENT LIABILITIES | | |
| Current portion of long-term debt | \$ 2,654,019 | \$ 2,688,396 |
| Accounts payable | 872,679 | 459,836 |
| Accrued compensation | 359,596 | 279,755 |
| Other accrued liabilities | 188,098 | 168,066 |
| Total current liabilities | <u>4,074,392</u> | <u>3,596,053</u> |
| COMMITMENTS AND CONTINGENCIES | | |
| STOCKHOLDERS' EQUITY | | |
| Preferred stock, par value \$.10 per share; authorized 250,000 shares; issued none | — | — |
| Common stock, par value \$.10 per share; authorized 4,750,000 shares; issued and outstanding 1,977,104 shares in 2021 and 1,976,354, in 2020 | 197,710 | 197,635 |
| Additional paid-in-capital | 2,787,733 | 2,743,930 |
| Retained earnings | 8,576,142 | 8,897,781 |
| Total stockholders' equity | <u>11,561,585</u> | <u>11,839,346</u> |
| Total liabilities and stockholders' equity | <u>\$ 15,635,977</u> | <u>\$ 15,435,399</u> |

See notes to condensed financial statements.

IKONICS CORPORATION
CONDENSED STATEMENTS OF OPERATIONS (Unaudited)

| | Three Months Ended | |
|--|---------------------------|---------------------|
| | March 31, | |
| | 2021 | 2020 |
| NET SALES | \$ 3,073,408 | \$ 3,497,192 |
| COST OF GOODS SOLD | <u>2,077,076</u> | <u>2,343,960</u> |
| GROSS PROFIT | 996,332 | 1,153,232 |
| SELLING, GENERAL AND ADMINISTRATIVE EXPENSES | 1,183,591 | 1,781,020 |
| RESEARCH AND DEVELOPMENT EXPENSES | <u>134,922</u> | <u>183,580</u> |
| LOSS FROM OPERATIONS | (322,181) | (811,368) |
| INTEREST EXPENSE | (19,842) | (21,484) |
| OTHER INCOME | <u>37</u> | <u>6,917</u> |
| LOSS BEFORE INCOME TAXES | (341,986) | (825,935) |
| INCOME TAX BENEFIT | <u>(20,347)</u> | <u>(238,929)</u> |
| NET LOSS | <u>\$ (321,639)</u> | <u>\$ (587,006)</u> |
| LOSS PER COMMON SHARE | | |
| Basic | \$ (0.16) | \$ (0.30) |
| Diluted | <u>\$ (0.16)</u> | <u>\$ (0.30)</u> |
| WEIGHTED AVERAGE COMMON SHARES OUTSTANDING | | |
| Basic | <u>1,976,771</u> | <u>1,976,354</u> |
| Diluted | <u>1,976,771</u> | <u>1,976,354</u> |

See notes to condensed financial statements.

IKONICS CORPORATION

STATEMENTS OF STOCKHOLDERS' EQUITY
THREE MONTHS ENDED MARCH 31, 2021 and 2020 (unaudited)

For the three months ended March 31, 2021:

| | Common Stock | | Additional Paid-in Capital | Retained Earnings | Total Stock- holders' Equity |
|--|------------------|-------------------|----------------------------------|----------------------|---------------------------------------|
| | Shares | Amount | | | |
| BALANCE AT DECEMBER 31, 2020 | 1,976,354 | \$ 197,635 | \$ 2,743,930 | \$ 8,897,781 | \$ 11,839,346 |
| Net loss | — | — | — | (321,639) | (321,639) |
| Exercise of stock options and net of related tax benefit | 750 | 75 | 6,316 | — | 6,391 |
| Stock based compensation | — | — | 37,487 | — | 37,487 |
| BALANCE AT MARCH 31, 2021 | <u>1,977,104</u> | <u>\$ 197,710</u> | <u>\$ 2,787,733</u> | <u>\$ 8,576,142</u> | <u>\$ 11,561,585</u> |

For the three months ended March 31, 2020:

| | Common Stock | | Additional Paid-in Capital | Retained Earnings | Total Stock- holders' Equity |
|------------------------------|------------------|-------------------|----------------------------------|----------------------|---------------------------------------|
| | Shares | Amount | | | |
| BALANCE AT DECEMBER 31, 2019 | 1,976,354 | \$ 197,635 | \$ 2,721,962 | \$ 9,337,101 | \$ 12,256,698 |
| Net loss | — | — | — | (587,006) | (587,006) |
| Stock based compensation | — | — | 3,688 | — | 3,688 |
| BALANCE AT MARCH 31, 2020 | <u>1,976,354</u> | <u>\$ 197,635</u> | <u>\$ 2,725,650</u> | <u>\$ 8,750,095</u> | <u>\$ 11,673,380</u> |

See notes to condensed financial statements.

IKONICS CORPORATION
CONDENSED STATEMENTS OF CASH FLOWS (Unaudited)

| | Three Months Ended | |
|---|----------------------------|----------------------------|
| | March 31, | |
| | 2021 | 2020 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net loss | \$ (321,639) | \$ (587,006) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: | | |
| Depreciation | 160,561 | 167,623 |
| Amortization | 9,000 | 9,454 |
| Stock based compensation | 37,487 | 3,688 |
| Net gain on sale and disposal of equipment | — | (2,324) |
| Changes in working capital components: | | |
| Trade receivables | 573,686 | 674,552 |
| Inventories | (316,941) | (408,233) |
| Prepaid expenses and other assets | (84,926) | 578,479 |
| Income tax receivable | 201,409 | (244,254) |
| Accounts payable | 412,843 | 1,575 |
| Accrued expenses | 99,875 | (620,830) |
| Net cash provided by (used in) operating activities | <u>771,355</u> | <u>(427,276)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchases of property and equipment | — | (135,125) |
| Proceeds from sales of equipment | — | 18,297 |
| Purchases of intangible assets | (6,787) | (3,423) |
| Proceeds on sale of short-term investments | — | 1,225,000 |
| Net cash (used in) provided by investing activities | <u>(6,787)</u> | <u>1,104,749</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Payment on long-term debt | (36,826) | (35,682) |
| Proceeds from exercise of stock options | 6,682 | — |
| Net cash used in financing activities | <u>(30,144)</u> | <u>(35,682)</u> |
| NET INCREASE IN CASH | 734,424 | 641,791 |
| CASH AT BEGINNING OF PERIOD | <u>3,693,845</u> | <u>963,649</u> |
| CASH AT END OF PERIOD | <u>\$ 4,428,269</u> | <u>\$ 1,605,440</u> |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION | | |
| Cash paid for interest | <u>\$ 17,960</u> | <u>\$ 19,105</u> |
| Cash received (paid for) income taxes, net | <u>\$ 221,756</u> | <u>\$ (5,325)</u> |

See notes to condensed financial statements.

IKONICS CORPORATION
NOTES TO CONDENSED FINANCIAL STATEMENTS

(Unaudited)

1. Basis of Presentation

The condensed balance sheet of IKONICS Corporation (the “Company”) as of March 31, 2021, and the related condensed statements of operations for the three months ended March 31, 2021 and 2020, the condensed statements of stockholders' equity for the three months ended March 31, 2021 and 2020, and condensed cash flows for the three months ended March 31, 2021 and 2020, have been prepared without being audited.

In the opinion of management, these statements reflect all adjustments (consisting of only normal recurring adjustments) necessary to present fairly the financial position of IKONICS Corporation as of March 31, 2021, and the results of operations and cash flows for all periods presented.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted. Therefore, these statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2020.

The results of operations for interim periods are not necessarily indicative of results that will be realized for the full fiscal year.

The Company relies on cash flow generated from operations and available borrowings under its bank line of credit to fund its working capital and other operating and investing needs. The Company's ability to borrow under the bank line of credit is based on its ability to continue to renew the maturity date of the bank line of credit.

The global, regional and local spread of COVID-19 has resulted in significant global mitigation measures, including government-directed quarantines, social distancing and shelter-in-place mandates, travel restrictions and/or bans, and restricted access to certain corporate facilities and manufacturing sites. Uncertainty with respect to the severity and duration of the pandemic has contributed to periods of volatility and disruption of financial markets. While the severity and duration of the COVID-19 pandemic remain uncertain, impacts to the Company may include, but are not limited to: fluctuations in the Company's stock price due to market volatility; a decrease in demand for the Company's products; reduced profitability; supply chain disruptions impeding the Company's ability to ship and/or receive product; potential interruptions or limitations to manufacturing operations imposed by local, state or federal governments; shortages of key raw materials; workforce absenteeism and distraction; labor shortages; customer credit concerns; cyber security and data accessibility disruptions due to remote working arrangements; reduced sources of liquidity; increased borrowing costs; and potential asset impairment charges. Business disruptions and market volatility resulting from the COVID-19 pandemic could continue to have a material adverse impact on the Company's results of operations, financial condition and cash flows.

Based on the Company's current cash position, and expected future cash flows, the Company believes it will have sufficient cash to fund its operations beyond twelve months from the date of the issuance of the accompanying unaudited condensed financial statements.

2. Inventories

The major components of inventories as of March 31, 2021 and December 31, 2020 were as follows:

| | <u>Mar 31, 2021</u> | <u>Dec 31, 2020</u> |
|------------------------|---------------------|---------------------|
| Raw materials | \$ 1,339,843 | \$ 1,323,655 |
| Work-in-progress | 448,424 | 428,753 |
| Finished goods | 1,357,647 | 1,065,458 |
| Reduction to LIFO cost | <u>(1,183,998)</u> | <u>(1,172,891)</u> |
| Total Inventories | <u>\$ 1,961,916</u> | <u>\$ 1,644,975</u> |

3. Earnings Per Common Share (EPS)

Basic EPS is calculated using net loss divided by the weighted average of common shares outstanding. Diluted EPS is calculated similarly to Basic EPS except that the weighted average number of common shares outstanding is increased to include the number of additional common shares that would have been outstanding if the potential dilutive common shares, such as those shares subject to options, had been issued. The options and restricted stock units disclosed in Note 4 have been excluded from the computation because of their antidilutive effect.

Shares used in the calculation of diluted EPS are summarized below:

| | <u>Three Months Ended</u> | |
|--|---------------------------|---------------------|
| | <u>Mar 31, 2021</u> | <u>Mar 31, 2020</u> |
| Weighted average common shares outstanding | 1,976,771 | 1,976,354 |
| Dilutive effect of stock options and restricted stock units | — | — |
| Weighted average common and common equivalent shares outstanding | <u>1,976,771</u> | <u>1,976,354</u> |

IKONICS CORPORATION
NOTES TO CONDENSED FINANCIAL STATEMENTS

(Unaudited)

If the Company was in a net income position for the first three months of 2021, 15,000 options with a weighted average exercise price of \$6.43 would have been included as part of the computation of common share equivalents as the options would have been dilutive, while 11,750 options with a weighted average exercise price of \$11.39 would have remained excluded because these options were anti-dilutive.

If the Company was in a net income position for the first three months of 2021, 55,800 restricted stock units would have been included as part of the computation of common share equivalents as the restricted stock units would have been dilutive.

If the Company was in a net income position for the first three months of 2020, the computation of diluted income per share would exclude 23,750 options with a weighted average exercise price of \$8.01 because the inclusion of these options would be anti-dilutive.

4. Stock-Based Compensation

The Company maintains the 2019 Equity Incentive Plan (the "2019 Plan"). The 2019 Plan replaced the 1995 Incentive Stock Option Plan (the "1995 Plan") upon its ratification by shareholders in April 2019. The 1995 plan authorized the issuance of up to 442,750 shares of common stock through grants of restricted stock units and options. Of those shares, 4,250 were subject to outstanding options as of March 31, 2021. Awards granted under the 1995 Plan will remain in effect until they are exercised or expire according to their terms. At the time the 2019 Plan was approved, there were 102,157 shares reserved for future grants under the 1995 Plan which will no longer be available for future grants.

Under the terms of the 2019 Plan, the number of shares of common stock that may be the subject of awards and issued under the 2019 Plan was initially set at 102,157. Subsequent to the approval of the 2019 Plan, 11,750 outstanding options granted under the 1995 Plan were forfeited. Under the terms of the 2019 Plan, those forfeited options are added back to the 2019 Plan reserve pool. As of March 31, 2021, 55,800 restricted stock units (RSUs) and 23,250 options have been granted under the 2019 Plan, of which 750 stock options have been forfeited, bringing the number of shares of common stock available for future awards under the 2019 Plan to 35,607.

The Company charged compensation cost of approximately \$37,500 against the loss for the three months ended March 31, 2021 and approximately \$3,700 for the three months ended March 31, 2020. As of March 31, 2021, there was approximately \$396,000 of unrecognized compensation cost related to unvested share-based compensation awards. That cost is expected to be recognized over the next three years.

The Company receives a tax deduction for certain stock option exercises during the period in which the options are exercised, generally for the excess of the market price at the time the stock options are exercised over the exercise price of the options, which increases additional paid in capital and reduces income taxes payable.

Proceeds from the exercise of 750 stock options with an intrinsic value of approximately \$1,700 were approximately \$6,700 for the three months ended March 31, 2021. No stock options were exercised during the three months ended March 31, 2020.

There were 10,000 options granted during the three months ended March 31, 2021 and 2020. The fair value of options granted during the three months ended March 31, 2021 and 2020 were estimated using the Black Scholes option pricing model with the following assumptions:

| | 2021 | | 2020 | |
|---|---------|---|---------|---|
| Dividend yield | — | | — | |
| Expected volatility | 51.6 | % | 40.3 | % |
| Expected life of option (years) | 10 | | 10 | |
| Risk-free interest rate | 1.4 | % | 1.4 | % |
| Fair value of each option on grant date | \$ 7.05 | | \$ 2.90 | |

Stock option activity during the three months ended March 31, 2021 was as follows:

| | Shares | Weighted Average Exercise Price |
|--------------------------------|--------|--|
| Outstanding at January 1, 2021 | 17,500 | \$ 6.97 |
| Granted | 10,000 | 11.50 |
| Exercised | (750) | 8.91 |
| Expired and forfeited | — | — |
| Outstanding at March 31, 2021 | 26,750 | \$ 8.61 |
| Exercisable at March 31, 2021 | 7,915 | \$ 7.73 |

The aggregate intrinsic value of all options outstanding and for those exercisable at March 31, 2021 was approximately \$59,600 and \$21,700, respectively.

There were 1,500 RSUs granted during the three months ended March 31, 2021. The shares underlying the awards were assigned a weighted average value of \$9.85 per share, which was the closing price of the Company's common stock on the date of grants. These awards are scheduled to vest over three years. No RSUs were granted during the three months ended March 31, 2020.

RSU activity during the three months ended March 31, 2021 is summarized as follows:

| | Number of Shares | Weighted Average Grant Date Fair Value |
|------------------------------------|-----------------------------|---|
| Unvested shares at January 1, 2021 | 54,300 | \$ 6.11 |
| Granted | 1,500 | 9.85 |
| Vested | — | — |
| Forfeited or surrendered | — | — |
| Unvested shares at March 31, 2021 | <u>55,800</u> | <u>6.21</u> |

IKONICS CORPORATION
NOTES TO CONDENSED FINANCIAL STATEMENTS

(Unaudited)

5. Segment Information

The Company's reportable segments are strategic business units that offer different products and have varied customer bases. There are four reportable segments: Chromaline, IKONICS Imaging, Digital Texturing (DTX) and Advanced Material Solutions (AMS). Chromaline sells screen printing film, emulsions, and inkjet receptive film primarily to distributors and some end users. IKONICS Imaging sells photo resistant film, art supplies, glass, and related abrasive etching equipment to both end users and distributors. AMS provides sound deadening and weight reduction technology to the aerospace industry along with products and services for etched composites, ceramics, glass and silicon wafers. DTX includes products and customers related to patented and proprietary inkjet technology used for mold texturing and prototyping. The accounting policies applied to determine the segment information are the same as those described in the Company's Annual Report on Form 10-K for the year ended December 31, 2020.

Management evaluates the performance of each segment based on the components of divisional income (loss). Assets and liabilities are not allocated to segments, except for trade receivables. Financial information with respect to the reportable segments follows:

For the three months ended March 31, 2021:

| | IKONICS | | | | | Total |
|-------------------------------------|-------------------|-------------------|-----------------|--------------------|---------------------|---------------------|
| | Chromaline | Imaging | DTX | AMS | Unalloc. | |
| Net sales | \$ 1,698,681 | \$ 1,086,601 | \$ 76,311 | \$ 211,815 | \$ — | \$ 3,073,408 |
| Cost of goods sold | 1,234,785 | 549,655 | 42,792 | 249,844 | — | 2,077,076 |
| Gross profit (loss) | 463,896 | 536,946 | 33,519 | (38,029) | — | 996,332 |
| Selling general and administrative* | 258,002 | 216,536 | 30,039 | 58,621 | 620,393 | 1,183,591 |
| Research and development* | — | — | — | — | 134,922 | 134,922 |
| Income (loss) from operations | <u>\$ 205,894</u> | <u>\$ 320,410</u> | <u>\$ 3,480</u> | <u>\$ (96,650)</u> | <u>\$ (755,315)</u> | <u>\$ (322,181)</u> |

For the three months ended March 31, 2020:

| | IKONICS | | | | | Total |
|-------------------------------------|-------------------|-------------------|------------------|--------------------|-----------------------|---------------------|
| | Chromaline | Imaging | DTX | AMS | Unalloc. | |
| Net sales | \$ 1,964,340 | \$ 970,099 | \$ 112,529 | \$ 450,224 | \$ — | \$ 3,497,192 |
| Cost of goods sold | 1,418,269 | 477,723 | 51,746 | 396,222 | — | 2,343,960 |
| Gross profit | 546,071 | 492,376 | 60,783 | 54,002 | — | 1,153,232 |
| Selling general and administrative* | 426,219 | 278,862 | 34,373 | 103,109 | 938,457 | 1,781,020 |
| Research and development* | — | — | — | — | 183,580 | 183,580 |
| Income (loss) from operations | <u>\$ 119,852</u> | <u>\$ 213,514</u> | <u>\$ 26,410</u> | <u>\$ (49,107)</u> | <u>\$ (1,122,037)</u> | <u>\$ (811,368)</u> |

*The Company does not allocate all selling, general and administrative expenses or any research and development expenses to its operating segments for internal reporting.

IKONICS CORPORATION
NOTES TO CONDENSED FINANCIAL STATEMENTS

(Unaudited)

Trade receivables by segment as of March 31, 2021 and December 31, 2020 were as follows:

| | <u>Mar 31, 2021</u> | <u>Dec 31, 2020</u> |
|-----------------|----------------------------|----------------------------|
| Chromaline | \$ 1,106,648 | \$ 1,676,592 |
| IKONICS Imaging | 247,725 | 396,116 |
| DTX | 33,388 | 35,983 |
| AMS | 181,975 | 57,676 |
| Unallocated | <u>(24,209)</u> | <u>(47,154)</u> |
| Total | <u><u>\$ 1,545,527</u></u> | <u><u>\$ 2,119,213</u></u> |

6. Income Taxes

The Company records its interim provision for income taxes by applying its estimated annual effective tax rate to the year-to-date pre-tax income and adjusting for discrete tax items recorded in the period. Deferred income taxes result from temporary differences between the reporting of amounts for financial statement purposes and income tax purposes. These differences relate primarily to different methods used for income tax reporting purposes, including for depreciation and amortization, warranty and vacation accruals, and deductions related to allowances for doubtful accounts receivable and inventory reserves. The provision for income taxes included current federal and state income tax expense, as well as deferred federal and state income tax expense.

Management assesses the available positive and negative evidence to estimate whether sufficient future taxable income will be generated to permit use of the existing deferred tax assets. A significant piece of objective negative evidence evaluated was the cumulative loss incurred over the three-year period ended March 31, 2021. Such objective evidence limits the ability to consider other subjective evidence, such as our projections for future growth.

On the basis of this evaluation, as of March 31, 2021, a full valuation allowance has been recorded to reserve for deferred tax assets entirely, which are not expected to be realized. The valuation allowance will be reevaluated on a quarterly basis and may change if estimates of future taxable income during the carryforward period is increased or if objective negative evidence in the form of cumulative losses is no longer present and additional weight is given to subjective evidence such as our projections for growth.

The effective tax rate for the three months ended March 31, 2021 was a benefit of 5.9%, compared to a benefit 28.9% for the three months ended March 31, 2020. The primary driver of the change in the Company's effective tax rate is attributable to additional benefit from an net operating loss carryback claim recorded in the prior year. The Company recorded an income tax benefit of \$20,000 and a benefit of \$239,000 for the three months ended March 31, 2021 and 2020, respectively.

IKONICS CORPORATION
NOTES TO CONDENSED FINANCIAL STATEMENTS

(Unaudited)

The Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority is more-likely -than-not to sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the condensed consolidated financial statements is the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with the relevant tax authority. As of March 31, 2021, the Company has no unrecognized tax benefits.

This Company is not currently under examination in any jurisdiction. In the event of any future tax assessments, the Company has elected to record the income taxes and any related interest and penalties as income tax expense on the statement of operations.

7. Long-Term Debt

Duluth Economic Development Authority Loan

On April 1, 2016, the Company entered into a financing agreement (the “Financing Agreement”) under which the Duluth Economic Development Authority (the “Issuer”) agreed to sell \$3,415,000 of its Tax Exempt Industrial Revenue Bonds, Series 2016 (IKONICS Project) (the “Bonds”) to Wells Fargo Bank, National Association (the “Bank”), and the Bank agreed to lend to the Company the proceeds received from the sale of the Bonds (the “Loan”). The closing of the sale of the Bonds occurred on April 29, 2016. The proceeds from the Loan were used to finance the construction of a 27,300-square foot building as well as related equipment for use in the Company’s manufacture of sound deadening technology used in the aerospace industry and products consisting of etched composites, ceramics, glass and silicon wafers, to be located in Duluth, Minnesota (the “Project”). The Loan requires monthly payments of approximately \$18,000, including interest. The Loan bears interest at a rate of 2.60% per year, subject to change based upon changes to the maximum federal corporate tax rate. Including debt costs of approximately \$139,000, the Loan’s effective interest rate was 3.23% at March 31, 2021.

The Company is subject to certain customary covenants set forth in the associated covenant agreement, including a requirement that the Company maintain a debt service coverage ratio of not less than 1.25 to 1.00.

The Loan was subject to mandatory purchase provisions, under which any owners of the Bonds (the “Owners”) can tender the Bonds to the Issuer on April 1, 2021, resulting in the Company repaying the outstanding loan principal and any outstanding accrued and unpaid interest to the Issuer at that time. During the first three months of 2021, the Company was informed that the bank will require the Company to repay the outstanding principal and any outstanding accrued and unpaid interest on April 1, 2021. On April 1, 2021, the Company repaid the entire loan including principal amount of \$2.7 million and interest of \$6,100 with existing cash on hand. As of March 31, 2021, the Company classified the entire Loan as a current liability.

Line of Credit

The Company also has a bank line of credit providing for borrowings of up to \$2,050,000 which expires on August 30, 2021 and bears interest at 1.8 percentage points over the 30-day LIBOR rate. The Company did not utilize this line of credit during the first three months of 2021 or 2020 and there were no borrowings outstanding as of March 31, 2021 or December 31, 2020. There are no financial covenants related to the line of credit.

Both the \$3,415,000 financing pursuant to the Loan and the line of credit are collateralized by substantially all assets of the Company.

IKONICS CORPORATION

Cautionary Note Regarding Forward-Looking Statements

The information presented below in Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements within the meaning of the safe harbor provisions of Section 21E of the Securities Exchange Act of 1934, as amended. Statements that are not historical or current facts, including statements about beliefs and expectations, are forward-looking statements. These forward-looking statements include but are not limited to statements relating to our future plans, objectives and results and the impact of the COVID-19 pandemic on our financial results and the effectiveness of the Company's responses to the pandemic. Such statements are subject to risks and uncertainties, including those discussed elsewhere in this report and under the heading "Risk Factors" in Part I, Item 1A of our [Annual Report on Form 10-K for the year ended December 31, 2020](#), as updated in our subsequent reports filed with the SEC, which could cause actual results to differ materially from those projected. Because actual results may differ, readers are cautioned not to place undue reliance on these forward-looking statements.

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following management's discussion and analysis focuses on those factors that had a material effect on the Company's financial results of operations during the first three months of 2021 and 2020. It should be read in connection with the Company's condensed unaudited financial statements and notes thereto included in this Form 10-Q.

Impact of the COVID-19 Pandemic

The Company is closely monitoring the coronavirus (COVID-19) pandemic and its impact on its business. The outbreak and continuing spread of COVID-19 has resulted in a substantial curtailment of business activities worldwide and is causing weakened economic conditions, both nationally and globally. As part of efforts to contain the spread of COVID-19, state, local and foreign governments have imposed various restrictions on the conduct of business and travel. Government restrictions, such as stay-at-home orders and quarantines and company remote work policies have led to a significant number of business closures and slowdowns. These business closures and slowdowns have already adversely impacted and will likely continue to adversely impact the Company directly, as well as cause its customers and suppliers to slow or stop production, which will likely significantly disrupt the Company's sales, production and supply chain. For example, as a result of the COVID-19 pandemic, the Company began to experience decreased demand for its products and services during the year ended 2020. The Company anticipates a sustained decrease in global demand from pre-COVID-19 levels for certain of its products and services during 2021. This decrease in demand will likely have a material adverse impact on the Company's business, operating results and financial condition. The Company's facilities continue to operate and are doing so safely, having implemented social distancing and enhanced health, safety and sanitization measures. The Company's leadership continues to address the situation and is adjusting as necessary. The Company has also implemented necessary procedures to enable a significant portion of its employee base to work remotely. As the situation continues to evolve into a more prolonged pandemic, the Company expects the COVID-19 pandemic to have a significant adverse effect on economies and financial markets globally, potentially leading to a significant worldwide economic downturn, which could have a significant adverse effect on the Company's business, operating results and financial condition. However, the duration of these trends and the magnitude of such impacts cannot be precisely estimated at this time, as they are affected by a number of factors (some of which are outside management's control), including those presented in Part II, Item 1A. "Risk Factors" below. To partially mitigate the negative impact of the COVID-19 pandemic, in 2020 the Company implemented cost reduction efforts including a reduction of its workforce, a decrease in the Company's contribution to its 401(k) retirement plan and the elimination of all non-essential expenditures.

Critical Accounting Estimates

The Company prepares its financial statements in conformity with accounting principles generally accepted in the United States of America. Therefore, the Company is required to make certain estimates, judgments and assumptions that the Company believes are reasonable based upon the information available. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods presented. The accounting estimates, which the Company believes are the most critical to aid in fully understanding and evaluating its reported financial results, include the following:

Trade Receivables. The Company performs ongoing credit evaluations of its customers and adjusts credit limits based upon payment history and the customer's current credit worthiness, as determined by review of the current credit information. The Company continuously monitors collections and payments from its customers and maintains a provision for estimated credit losses based upon historical experience and any specific customer collection issues that have been identified. While such credit losses have historically been within expectations and the provisions established, the Company cannot guarantee that it will continue to experience the same collection history that has occurred in the past especially given the unpredictability of any effects related to the COVID-19 pandemic. The general payment terms are net 30-45 days for domestic customers and net 30-90 days for foreign customers. A small percentage of the trade receivables balance is denominated in a foreign currency with no concentration in any given country. At the end of each reporting period, the Company analyzes the receivable balance for customers paying in a foreign currency. These balances are adjusted to each quarter or year-end spot rate in accordance with FASB ASC 830, *Foreign Currency Matters*. The Company also maintains a provision for any customer related returns based upon historical experience of actual returns and any specifically identified product issues, refunds or credits.

Inventories. Inventories are valued at the lower of cost or net realizable value using the last in, first out (LIFO) method. The Company monitors its inventory for obsolescence and records reductions from cost when required.

Income Taxes. Deferred taxes are provided on a liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carryforwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. Deferred tax assets and liabilities are presented as long-term on a net basis. The Company follows the accounting standard on accounting for uncertainty in income taxes, which addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under this guidance, the Company may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement. The guidance on accounting for uncertainty in income taxes also addresses derecognition, classification, interest and penalties on income taxes, and accounting in interim periods.

Revenue recognition. Revenue is measured based on consideration specified in the contract with a customer, adjusted for any applicable estimates of variable consideration and other factors affecting the transaction price, including noncash consideration, consideration paid or payable to customers and significant financing components. While most of the Company's revenue is contracted with customers through one-time purchase orders and short-term contracts, the Company does have long-term arrangements with certain customers. Revenue from all customers is recognized when a performance obligation is satisfied by transferring control of a distinct good or service to a customer.

Individually promised goods and services in a contract are considered a distinct performance obligation and accounted for separately if the customer can benefit from the individual good or service on its own or with other resources that are readily available to the customer and the good or service is separately identifiable from other promises in the arrangement. When an arrangement includes multiple performance obligations, the consideration is allocated between the performance obligations in proportion to their estimated standalone selling price. Costs related to products delivered are recognized in the period incurred, unless criteria for capitalization of costs are met. Costs of revenues consist primarily of direct labor, manufacturing overhead, materials and components. The Company does not incur significant upfront costs to obtain a contract. If costs to obtain a contract were to become material, the costs would be recorded as an asset and amortized to expense in a manner consistent with the related recognition of revenue.

The Company excludes governmental assessed and imposed taxes on revenue transactions that are invoiced to customers from revenue. The Company includes freight billed to customers in revenue. Shipping and handling costs associated with outbound freight after control over a product has transferred to a customer are accounted for as a fulfillment cost and are included in cost of goods sold.

The timing of revenue recognition, billings and cash collections results in accounts receivable on the balance sheet.

Performance obligations. A performance obligation is a promise in a contract to transfer a distinct good or service to the customer. A contract's transaction price is allocated to each distinct performance obligation in proportion to its standalone selling price and recognized as revenue when, or as, the performance obligation is satisfied. The Company's various performance obligations and the timing or method of revenue recognition are discussed below:

The Company sells its products to both distributors and end-users. Each unit of product delivered under a customer order represents a distinct and separate performance obligation as the customer can benefit from each unit on its own or with other resources that are readily available to the customer and each unit of product is separately identifiable from other products in the arrangement.

The transaction price for the Company's products is the invoiced amount. The Company does not have variable consideration in the form of refunds, credits, rebates, price concessions, pricing incentives or other items impacting transaction price. The purchase order pricing in arrangements with customers is deemed to approximate standalone selling price; therefore, the Company does not need to allocate proceeds on a relative standalone selling price allocation between performance obligations. The Company applies the practical expedient in FASB ASC 606-10-50-14 and does not disclose information about remaining performance obligations that have original expected durations of one year or less. There are no material obligations that extend beyond one year.

Revenue is recognized when transfer of control occurs as defined by the terms in the customer agreement. The Company immediately recognizes incidental items that are immaterial in the context of the contract. The Company has also applied the practical expedient in FASB ASC 606-10-32-18 regarding the adjustment of the promised amount of consideration for the effects of a significant financing component when the customer pays for that good or service within one year or less, as the Company does not have any significant financing components in its customer arrangements as payment is received at or shortly after the point of sale, generally thirty to ninety days.

The Company estimates returns based on an analysis of historical experience if the right to return products is granted to its customers. The Company does not record a return asset as non-conforming products are generally not returned. The Company's return policy does not vary by geography. The customer has no rotation or price protection rights. The Company is not under a warranty obligation except as described below.

Sales commissions. Sales commissions paid to sales representatives are eligible for capitalization as they are incremental costs that would not have been incurred without entering into a specific sales arrangement and are recoverable through the expected margin on the transaction. The Company has elected to apply the practical expedient provided by FASB ASC 340-40-25-4 and recognize the incremental costs of obtaining contracts as an expense when incurred, as the amortization period of the assets that would have otherwise been recognized is one year or less. The Company records these costs in selling, general, and administrative expense.

Product warranty. The Company offers warranties on various products and services. These warranties are assurance type warranties that are not sold on a standalone basis; therefore, they are not considered distinct performance obligations. The Company estimates the costs that may be incurred under its warranties and records a liability in the amount of such costs at the time the revenue is recognized for the product sale.

International revenue. The Company markets its products to numerous countries in North America, Europe, Latin America, Asia and other parts of the world. Foreign sales were approximately 27% of total sales during the first three months of 2021 and 31% during the first three months of 2020.

Results of Operations

Quarter Ended March 31, 2021 Compared to Quarter Ended March 31, 2020

Sales. The Company's 2021 first quarter sales of \$3.1 million were \$424,000, or 12.1%, lower than the 2020 first quarter sales of \$3.5 million. Chromaline's 2021 first quarter sales of \$1.7 million decreased by 13.5% from first quarter 2020 sales of \$2.0 million while AMS sales decreased from \$450,000 in the first quarter of 2020 to \$212,000 in the first quarter of 2021, a 53.0% decrease. DTX sales also decreased by 32.2% in the first quarter of 2021 to \$76,000 compared to \$113,000 in the first quarter of 2020. Chromaline, AMS and DTX sales continue to be negatively impacted by the slowdown in economic activity related to the COVID-19 pandemic. Partially offsetting these decreases, IKONICS Imaging sales increased from \$970,000 in the first quarter of 2020 to \$1.1 million in the first quarter of 2021, a 12.0% increase. The IKONICS Imaging sales increase is related to improving IKONART® sales. IKONICS anticipates that the COVID-19 outbreak will continue to adversely impact sales in all of its divisions for most of 2021 due to decreased demand for certain of its products and services.

Gross Profit. Gross profit was \$996,000 or 32.4% of sales, in the first three months of 2021 compared to \$1.2 million, or 33.0%, of sales for the first three months of 2020. Lower sales and production volume, resulted in the Chromaline gross margin decreasing from 27.8% in the first quarter of 2020 to 27.3% in the first quarter of 2021. A decrease in sales volumes also resulted in the AMS gross margin decreasing to a negative 18.0% in first three months of 2021 from 12.0% in the first three months of 2020. A large portion of the AMS cost structure is fixed, causing sales volumes to have a significant impact on its gross margin. The IKONICS Imaging 2021 first quarter gross margin decreased from 50.8% in 2020 to 49.4% in 2021 due to a less favorable sales mix while the DTX gross margin decreased from 54.0% in first three months of 2020 to 43.9% for the same period in 2021. The DTX gross margin decrease in the first quarter of 2021 was due to lower sales of high margin film sales and increased production costs. IKONICS anticipates that the COVID-19 outbreak will continue to adversely impact gross margins for most of 2021 due to lower sales volumes and production output.

Selling, General and Administrative Expenses. Selling, general and administrative expenses were \$1.2 million or 38.5% of sales, in the first quarter of 2021 compared to \$1.8 million, or 50.9% of sales, for the same period in 2020. Selling, general and administrative expenses for the first quarter of 2021 decreased primarily due to a reduction in personnel, travel, trade show, promotional and consulting expenses. Selling, general and administration expenses in the first quarter of 2020 were also unfavorably impacted by \$365,000 of one-time costs related to the Chief Executive Officer transition. These costs include severance payments, a signing bonus, relocation expenses and executive search consulting expenses.

Research and Development Expenses. Research and development expenses during the first quarter of 2021 were \$135,000, or 4.4% of sales, versus \$184,000, or 5.2%, of sales for the same period in 2020. Research and development expenses in the first quarter of 2021 were favorably impacted by a reduction in staffing levels.

Interest Expense. Interest expense for the first quarter of 2021 and 2020 was \$20,000 and \$21,000, respectively.

Income Taxes. For the three months ended March 31, 2021 the effective tax rate was a benefit of 5.9% , compared to a benefit of 28.9% for the three months ended March 31, 2020. The primary driver of the change in the Company's effective tax rate is attributable to additional benefit for a net operating loss carryback claim recorded in the prior year. The Company recorded an income tax benefit \$20,000 and \$239,000 for the three months ended March 31, 2021 and 2020, respectively.

Liquidity and Capital Resources

Outside of the building expansion, for which \$3.4 million in financing was obtained during 2016 and the \$1.2 million Paycheck Protection loan the Company received and was forgiven in 2020, the Company has financed its operations principally with funds generated from operations. These funds have historically been sufficient to cover the Company's normal operating expenditures, annual capital requirements, and research and development expenditures.

Cash was \$4.4 million and \$3.7 million at March 31, 2021 and December 31, 2020, respectively. Operating activities provided \$771,000 in cash during the first three months of 2021 compared to a use of cash of \$427,000 during the same period in 2020. Cash provided by or used in operating activities is primarily the result of net losses adjusted for non-cash depreciation, amortization, and certain changes in working capital components discussed in the following paragraph.

During the first three months of 2021, trade receivables decreased by \$574,000. This decrease was due primarily to a slowdown in sales of products and services during the first quarter of 2021. The Company believes that the quality of its receivables is high and that strong internal controls are in place to maintain proper collections. Inventories increased by \$317,000 due to higher finished goods levels. Prepaid expenses and other assets increased by \$85,000 reflecting the prepayment of insurance premiums. Accrued expenses increased \$100,000 due to the timing of payroll. Accounts payable increased by \$413,000 as the Company has increased inventory levels during the first quarter. Income taxes receivable decreased by \$201,000 as the Company received payment during the first quarter of 2021 on previously recorded income tax refund.

During the first three months of 2020, trade receivables decreased \$675,000. This decrease was due primarily to a slowdown in sales of products and services during the latter part of the 2020 first quarter, as a result of the aforementioned COVID-19 pandemic. The Company believes that the quality of its receivables is high and that strong internal controls are in place to maintain proper collections. Inventories increased by \$408,000 due to higher finished goods levels as the Company experienced lower than expected sales towards the end of the first quarter of 2020. Prepaid expenses and other assets decreased by \$578,000 reflecting a decrease in a receivable related to the reimbursement of 2019 medical insurance costs that the Company received from its stop-loss insurance carrier. Accrued expenses decreased \$621,000, reflecting a decrease in the accrual for health insurance costs. Accounts payable increased by \$2,000 due to the timing of vendor payments. Income taxes receivable increased by \$244,000 as the Company recognized an income tax benefit attributable to a net operating loss carryback claim.

During the first three months of 2021, cash used in investing activities was \$7,000 as during the three months of 2021, the Company incurred \$7,000 in patent application costs that the Company records as an asset and amortizes upon successful completion of the application process.

During the first three months of 2020, cash provided by investing activities was \$1.1 million. Five certificates of deposits totaling \$1.2 million matured during the first three months of 2020. The Company's purchases of equipment of \$135,000 were mainly for improvements to production and process capabilities and to replace a vehicle. The Company received \$18,000 in proceeds from the sale of a vehicle. Also, during the first three months of 2020, the Company incurred \$3,000 in patent application costs that the Company records as an asset and amortizes upon successful completion of the application process.

On April 1, 2016, the Company entered into a financing agreement (the "Financing Agreement") under which the Duluth Economic Development Authority (the "Issuer") agreed to sell \$3,415,000 of its Tax Exempt Industrial Revenue Bonds, Series 2016 (IKONICS Project) (the "Bonds") to Wells Fargo Bank, National Association (the "Bank"), and the Bank agreed to lend to the Company the proceeds received from the sale of the Bonds (the "Loan"). Related to the Company's Loan, the Company made principal payments of \$37,000 during the first three months of 2021 and \$36,000 during the first three months of 2020.

The Company was subject to certain customary covenants set forth in the Loan, including a requirement that the Company maintain a debt service coverage ratio of not less than 1.25 to 1.00. As of December 31, 2020, the Company was in compliance with the debt service coverage ratio loan covenant. During the first quarter of 2021, the Company was notified by the bank that per the loan agreement the bank will recall the loan on April 1, 2021. On April 1, 2021, the Company repaid the entire loan including principal amount of \$2.7 million and interest of \$6,100 with existing cash on hand.

A bank line of credit providing for borrowings of up to \$2,050,000 expires August 30, 2021. The line of credit is collateralized by the Company's assets and bears interest at 1.8 percentage points over the 30-day LIBOR rate. The Company did not utilize this line of credit during the first three months of 2021 or 2020, and there were no borrowings outstanding as of March 31, 2021 or December 31, 2020. There are no financial covenants related to the line of credit.

The Company believes that current financial resources, its line of credit, and cash generated from operations, along with the Company's capacity for additional debt and/or equity financing will be sufficient to fund current and anticipated business operations. However, the full extent of the effect of the COVID-19 pandemic on the Company's customers, supply chain and business cannot be reasonably assessed at this time and the Company expects its full year 2021 results of operations to be adversely affected. The Company has developed a plan to mitigate the impact of COVID-19 which includes permanent reductions to the Company's workforce, temporary reductions in board and officer compensation, temporary suspension of the Company's contribution to its 401(k) retirement plan and the elimination of all non-essential expenditures. The impact of COVID-19 on the Company's operating results will depend on future developments, which are highly uncertain and cannot be predicted, including governmental and business reactions to the pandemic.

Capital Expenditures

Through the first three months of 2021, the Company had no capital expenditures.

The Company is planning capital expenditures in 2021 of approximately \$220,000 including improvements to the Company's production capabilities, process improvements, and information technology upgrades. Currently, the Company expects to fund its capital expenditures with existing cash and cash generated from operating activities.

International Activity

The Company markets its products to numerous countries in North America, Europe, Latin America, Asia and other parts of the world. Foreign sales were approximately 27% of total sales during the first three months of 2021 and 31% during the first three months of 2020. The fluctuations of certain foreign currencies have not significantly impacted the Company's operations, as the Company's foreign sales are not concentrated in any one region of the world, although a strong U.S. dollar does make the Company's products less competitive internationally. The Company believes its vulnerability due to uncertainties in foreign currency fluctuations and general economic conditions in foreign countries is not significant.

The Company's foreign transactions are primarily negotiated, invoiced and paid in U.S. dollars, while a portion is transacted in Euros. The Company has not implemented an economic hedging strategy to reduce the risk of foreign currency translation or transaction exposures, as management does not believe this to be a significant risk based on the scope and geographic diversity of the Company's foreign operations. Furthermore, the impact of foreign exchange on the Company's balance sheet and operating results was not material in either 2021 or 2020.

Future Outlook

See the discussion under the heading "Impact of the COVID-19 Pandemic" above for the Company's discussion of the COVID-19 pandemic.

IKONICS has spent an average of approximately 5% of annual sales in research and development and has made capital expenditures related to new products and programs. The Company plans to maintain its efforts in these areas to expedite internal product development as well as to form technological alliances with outside entities to commercialize new product opportunities.

The Company is also continuing to pursue DTX-related business initiatives. In addition to making efforts towards growing the inkjet technology business, the Company offers a range of products for creating texture surfaces and has introduced a fluid for use in prototyping. The Company is currently working on production improvements as part of its joint development agreement with AKK, a German manufacturer of high quality printers, to enhance its customer offerings. The Company has been awarded European, Japanese, and United States patents on its DTX technologies. The Company has also modified its DTX technology to facilitate entry into the market for prototyping.

The Company continues to make progress on its AMS business. The Company has three long-term sales agreements in place for its technology with major aerospace companies. However, based on customer communications, the Company anticipates reduced order volume for 2021 due to the COVID-19 pandemic.

Both the Chromaline and IKONICS Imaging units operate in mature markets. Although these business units require aggressive strategies to grow market share, both are developing new products and business relationships that the Company believes will contribute to growth. Early in 2019, the Company introduced its new IKONART® product to positive reviews and is generating sales. IKONART® provides a new way to make custom reusable stencils for the creative arts markets. In addition to its traditional emphasis on domestic markets, the Company will continue efforts to grow its business internationally by attempting to develop new markets and expanding market share where it has already established a presence. However, the strong U.S. dollar has made international growth challenging.

Other future activities undertaken to expand the Company's business may include strategic partnerships, acquisitions, building improvements, equipment additions, new product development and marketing opportunities.

Recent Accounting Pronouncements

In June 2016, the FASB issued ASU No. 2016-13, Measurement of Credit Losses on Financial Instruments, which revises guidance for the accounting for credit losses on financial instruments within its scope, and in November 2018, issued ASU No. 2018-19 and in April 2019, issued ASU No. 2019-04 and in May 2019, issued ASU No. 2019-05, and in November 2019, issued ASU No. 2019-11, which amended the standard. The new standard introduces an approach, based on expected losses, to estimate credit losses on certain types of financial instruments and modifies the impairment model for available-for-sale debt securities. The new approach to estimating credit losses (referred to as the current expected credit losses model) applies to most financial assets measured at amortized cost and certain other instruments, including trade and other receivables, loans, held-to-maturity debt securities, net investments in leases and off-balance-sheet credit exposures. This ASU is effective for fiscal years beginning after December 15, 2022, including interim periods within those fiscal years, with early adoption permitted. Entities are required to apply the standard's provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is adopted. The Company is still evaluating the impact of this ASU.

Off Balance Sheet Arrangements

The Company has no off-balance sheet arrangements.

ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

Not applicable

ITEM 4. Controls and Procedures

As of the end of the period covered by this report, the Company conducted an evaluation, under the supervision and with the participation of the principal executive officer and principal financial officer, of the Company's disclosure control and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")). Based on this evaluation, the principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and (ii) accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

There were no changes to the Company's internal control over financial reporting that occurred during the first three months of 2021 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

None

ITEM 1A. Risk Factors

You should carefully review and consider the information regarding certain factors which could materially affect the Company's business, financial condition or future results set forth under the heading "Risk Factors" in the Company's [Annual Report on Form 10-K for the fiscal year ended December 31, 2020](#). There have been no material changes or additions to the Company's risk factors discussed in such report, which could materially affect the Company's business, financial condition, or future results.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not applicable

ITEM 3. Defaults upon Senior Securities

Not applicable

ITEM 4. Mine Safety Disclosures

Not applicable

ITEM 5. Other Information

None

ITEM 6. Exhibits

The following exhibits are filed as part of this Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2021:

| Exhibit | Description |
|----------------|---|
| 3.1 | Restated Articles of Incorporation, as amended (Incorporated by reference to the Company's Current Report on Form 8-K filed on December 16, 2002). |
| 3.2 | By-Laws of the Company, as amended and restated on March 17, 2020 (Incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K filed on March 18, 2020). |
| 31.1 | Rule 13a-14(a)/15d-14(a) Certifications of CEO |
| 31.2 | Rule 13a-14(a)/15d-14(a) Certifications of CFO |
| 32 | Section 1350 Certifications |
| 101 | Interactive Data Files Pursuant to Rule 405 of Regulation S-T |

IKONICS CORPORATION

SIGNATURES

In accordance with the requirements of the Securities Exchange Act of 1934, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

IKONICS CORPORATION

DATE: May 13, 2021

By: /s/ Jon Gerlach
Jon Gerlach,
Chief Financial Officer, and
Vice President of Finance

RULE 13a-14(a)/15d-14(a) CERTIFICATIONS OF CEO

I, Glenn Sandgren, certify that:

1. I have reviewed this quarterly report on Form 10-Q of IKONICS Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15f and 15d-15(f)) for the registrant and we have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 13, 2021

/s/ Glenn Sandgren
Glenn Sandgren
Chief Executive Officer

RULE 13a-14(a)/15d-14(a)/CERTIFICATIONS OF CFO

I, Jon Gerlach, certify that:

1. I have reviewed this quarterly report on Form 10-Q of IKONICS Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15f and 15d-15(f)) for the registrant and we have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 13, 2021

/s/ Jon Gerlach

Jon Gerlach
Chief Financial Officer and Vice President of Finance

SECTION 1350 CERTIFICATIONS

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, each of the undersigned certifies that this periodic report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in this periodic report fairly presents, in all material respects, the financial condition and results of operations of IKONICS Corporation.

Date: May 13, 2021

/s/ Glenn Sandgren
Glenn Sandgren
Chief Executive Officer

Date: May 13, 2021

/s/ Jon Gerlach
Jon Gerlach
Chief Financial Officer and Vice President of Finance
