IKONICS CORP
Form 10QSB
August 14, 2003

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

FORM 10-QSB

(Mark One)

[X] Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the Quarterly Period Ended June 30, 2003

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 small business issuer as specified in its charter)

Minnesota	41-0730027
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification no.)
4832 Grand Avenue Duluth, Minnesota	55807
(Address of principal executive offices)	(Zip code)

(218) 628-2217

Issuer's telephone number

Not Applicable

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

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act 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 [X] No [ ]

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practical date: Common Stock, $.10 par value - 1,248,127 shares outstanding as of July 18, 2003.

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

IKONICS CORPORATION

QUARTERLY REPORT ON FORM 10-QSB

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PART I -- FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

IKONICS CORPORATION
BALANCE SHEETS

	JUNE 30 2003 (UNAUDITED)	DECEMBER 2002
ASSETS		

CURRENT ASSETS:		
Cash and cash equivalents	$ 821,853	$ 384,1
Marketable securities	251,531	246,0
Trade receivables, less allowance for doubtful accounts of $150,000 and $100,000, respectively	2,063,497	1,933,7
Inventories	1,924,240	1,771,9
Prepaid expenses and other assets	66,259	89,9
Income tax refund receivable	-	122,4
Deferred taxes	82,000	82,0
Total current assets	5,209,380	4,630,2
PROPERTY, PLANT, AND EQUIPMENT, at cost:		
Land, building and leasehold improvements	1,370,243	1,355,5
Machinery and equipment	2,281,818	2,231,4
Office equipment	1,171,033	1,144,5
Vehicles	167,783	167,1
	4,990,877	4,898,7
Less accumulated depreciation	3,837,980	3,694,1
	1,152,897	1,204,6
PATENTS, net of amortization of $46,306 and $41,800 respectively	113,530	90,9
NONCOMPETE AGREEMENT, net of amortization of $20,000 and $16,666 respectively	80,000	83,3
LICENSE AGREEMENTS, net of amortization of $6,562 and $2,500 respectively	93,438	97,5
OTHER ASSETS	112,834	187,5
DEFERRED TAXES	118,000	118,0
	$ 6,880,079	$ 6,412,1
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 605,674	$ 317,2
Accrued compensation	186,539	204,6
Accrued corporate income taxes	4,614	
Other accrued expenses	30,430	23,6
Total current liabilities	827,257	545,4
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 1,248,127 shares in 2003 and 2002	124,813	124,8
Additional paid-in capital	1,269,489	1,269,4
Retained earnings	4,670,052	4,483,8
Accumulated other comprehensive income (loss)	(11,532)	(11,5
Total stockholders' equity	6,052,822	5,866,6
	$ 6,880,079	$ 6,412,1

See notes to financial statements.

IKONICS CORPORATION
STATEMENTS OF OPERATIONS (UNAUDITED)

	THREE MONTHS ENDED JUNE 30		SIX ENDE
	2003	2002	2003
SALES	$3,161,731	$ 3,164,255	$5,992,378
COSTS AND EXPENSES:			
Cost of goods sold	1,689,079	1,771,311	3,314,937
Selling, general, and administrative	1,050,256	1,015,296	2,053,951
Research and development	174,898	187,263	343,222
	2,914,233	2,973,870	5,712,110
INCOME FROM OPERATIONS	247,498	190,385	280,268
INTEREST EXPENSE	-	(170)	-
LOSS ON INVESTMENT	(74,666)	-	(74,666
INTEREST INCOME	2,778	9,997	15,666
INCOME BEFORE INCOME TAXES	175,610	200,212	221,268
FEDERAL AND STATE INCOME TAX EXPENSE	19,131	68,971	35,111
NET INCOME	$ 156,479	$ 131,241	$ 186,157
EARNINGS PER SHARE:			
Basic	$ 0.13	$ 0.11	$ 0.15
Diluted	$ 0.13	$ 0.11	$ 0.15
WEIGHTED AVERAGE COMMON SHARES ASSUMED OUTSTANDING:			
Basic	1,248,127	1,248,127	1,248,127
Diluted	1,254,299	1,248,127	1,253,071

See notes to financial statements.

IKONICS CORPORATION
STATEMENTS OF CASH FLOWS (UNAUDITED)

	SIX MONTHS ENDED JUNE 30	
	2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	$ 186,157	$ 154,288
Adjustments to reconcile net income to net cash provided by/(used in) operating activities:		
Depreciation	143,875	151,445
Amortization	11,902	8,360
(Gain) on sale of property and equipment	(5,500)	(19,632)
Loss on investment	74,666	-
Provision for doubtful accounts	50,000	22,600
Changes in working capital components:		
Decrease (increase) in:		
Trade receivables	(179,728)	(649,013)
Inventories	(152,335)	(132,304)
Prepaid expenses and other assets	23,678	(114,993)
(Decrease) increase in:		
Accounts payable	288,445	124,559
Accrued expenses	(11,298)	3,126
Income taxes payable	127,083	188,975
Net cash provided by/(used in) operating activities	556,945	(262,587)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(92,145)	(94,169)
Proceeds on sale of plant and equipment	5,500	-
Purchase of intangibles	(27,119)	(50,000)
Purchases of marketable securities	(4,235)	(4,176)
Net cash (used in) investing activities	(119,199)	(148,345)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from revolving credit agreement	-	150,000
Re-purchase of company stock	-	(72,492)
	-	77,508
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	437,746	(333,426)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	384,107	543,679
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 821,853	$ 210,253

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Income taxes paid (refunded)	$ 21,480	$(105,900)

See notes to financial statements.

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IKONICS CORPORATION

NOTES TO FINANCIAL STATEMENTS

(Unaudited)

1. Notes to Financial Statements

The balance sheet of IKONICS Corporation (the "Company") as of June 30, 2003, and the related statements of operations for the three and six months ended June 30, 2003 and 2002, and cash flows for the six months ended June 30, 2003 and 2002, 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 June 30, 2003, 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 Form 10-KSB for the year ended December 31, 2002.

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

2. Inventory

The major components of inventory at June 30, 2003 and December 31, 2002 are as follows:

	Jun 30, 2003	Dec 31, 2002
Raw materials	$1,079,196	$ 735,006
Work-in-progress	269,753	257,813
Finished goods	814,547	1,003,342
Reduction to LIFO cost	(239,256)	(224,256)
Total Inventory	$1,924,240	$1,771,905

3. Stockholders' Equity

		Six Months Ended June 30, 2003
Total Stockholders' Equity-December 31, 2002		$ 5,866,663
Net income	$ 186,157	
Unrealized gain on available-for-sale investments	2	
Comprehensive income		186,159
Total Stockholders' Equity-June 30, 2003		$ 6,052,822

4. Earnings Per Common Share (EPS)

Basic EPS is calculated using net income divided by the weighted average of common shares outstanding during the quarter. Diluted EPS is similar to Basic except that the weighted average of common shares

outstanding is increased to include the number of additional common shares that would have been outstanding if the dilutive potential common shares, such as options, had been issued.

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

	Three Jun 30, 200
Weighted average common shares outstanding	1,248,12
Dilutive effect of stock options	6,17
Weighted average common and common equivalent shares outstanding	1,254,29

	Six Mo Jun 30, 200
Weighted average common shares outstanding	1,248,12
Dilutive effect of stock options	4,94
Weighted average common and common equivalent shares outstanding	1,253,07

Options to purchase 161,608 and 150,029 shares of common stock were outstanding during the quarter ended June 30, 2003 and 2002, respectively. The options to purchase were excluded from the computation of common stock equivalents because they were anti-dilutive for the quarter ended June 30, 2002.

5. Employee Stock Plans

The Company has a stock-based compensation plan. The Company accounts for those plans under the recognition and measurement principles of APB Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. Accordingly, no stock-based employee compensation cost has been recognized, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share had compensation cost for all of the stock-based compensation plans been determined based on the grant date fair values of awards (the method described in FASB Statement No. 123, Accounting for Stock-Based Compensation):

	Six Months Ended		Three M
	Jun 30, 2003	Jun 30, 2002	Jun 30, 2003
Net income:			
As reported	$ 186,157	$ 154,288	$ 156,47
Deduct total stock-based employee compensation expense determined under fair value based method for all awards, net of tax	32,939	55,182	18,56
Pro forma	$ 153,218	$ 99,106	$ 137,91
Basic earnings per share:			
As reported	$ 0.15	$ 0.12	$ 0.1
Pro forma	$ 0.12	$ 0.08	$ 0.1
Diluted earnings per share:			
As reported	$ 0.15	$ 0.12	$ 0.1
Pro forma	$ 0.12	$ 0.08	$ 0.1

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6. Intangible Assets

Intangible assets consist primarily of patents, licenses and covenants not to compete arising from business combinations. Intangible assets are amortized on a straight-line basis over their estimated useful lives or terms of their agreement. Estimated amortization expense for each of the next five years is $24,000 annually. In connection with license agreements, the Company has agreed to pay royalties ranging from 3% to 5% on the future sales of products subject to the agreements.

7. New Accounting Standards

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities" (FAS 149). FAS 149 amends and clarifies financial accounting and reporting for derivative instruments including certain derivative instruments embedded in other contracts and for hedging activities under FAS 133. FAS 149 is effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003. The adoption of FAS 149 is not expected to have a material impact on our financial statements.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" (FAS 150). FAS 150 clarifies the accounting for certain financial instruments and characteristics of both liabilities and equity and requires that those instruments be classified as liabilities in statements of financial position. Previously, many of these financial instruments were classified as equity. FAS 150 is effective for all financial instruments entered into or modified after May 31, 2003 and is otherwise effective at the beginning of the first interim period after June 15, 2003. We do not expect the adoption of FAS 150 to have a material effect on our financial statements.

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IKONICS CORPORATION

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. Such statements are subject to risks and uncertainties, including those discussed under "Factors that May Affect Future Results" below, that 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. Certain forward-looking statements are indicated by italics.

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 second quarter of 2003, the six months ended June 30, 2003 and the same periods of 2002. It should be read in connection with the Company's unaudited financial statements and notes thereto included in this Form 10-QSB.

FACTORS THAT MAY AFFECT FUTURE RESULTS

Certain statements made in this Quarterly Report on Form 10-QSB, including those summarized below, are forward-looking statements within the meaning of the safe harbor provisions of Section 21E of the Securities Exchange Act of 1934, as amended, that involve risks and uncertainties, and actual results may differ. Factors that could cause actual results to differ include those identified below.

- The Company's belief that the quality of its receivables is high and that strong internal controls are in place to maintain proper collections--This belief may be impacted by domestic economic conditions, by economic, political, regulatory or social conditions in foreign markets, or by the failure of the Company to properly implement or maintain internal controls.

- The Company's expectation that capital expenditures during the remainder of 2003 will be funded with cash generated from operating activities--This expectation may be affected by changes in the Company's anticipated capital expenditure requirements resulting from unforeseen required maintenance or repairs. The funding of planned or unforeseen expenditures may also be affected by changes in anticipated operating results resulting from decreased sales or increased operating expenses.

- The belief that the Company's current financial resources, cash generated from operations and the Company's capacity for debt and/or equity financing will be sufficient to fund current and anticipated business operations and capital expenditures. The belief that the Company's low debt levels and available line of credit make it unlikely that a decrease in product demand would impair the Company's ability to fund operations--Changes in anticipated operating results, credit availability, equity market conditions or the Company's debt levels may further enhance or inhibit the Company's ability to maintain or raise appropriate levels of cash.

- The Company's belief that its vulnerability to foreign currency fluctuations and general economic conditions in foreign countries is not significant--This belief may be impacted by economic, political and social conditions in foreign markets and changes in regulatory and competitive conditions or a change in the amount or geographic focus of the Company's international sales.

- The Company's plans to continue to invest in research and development efforts, expedite internal product development and invest in technological alliances, as well as the expected focus and results of such investments--These plans and expectations may be impacted by general market conditions, unanticipated changes in expenses or sales, delays in the development of new products, technological

advances, the ability to find suitable and willing technology partners or other changes in competitive or market conditions.

- The Company's efforts to grow its international business--These efforts may be impacted by economic, political and social conditions in current and anticipated foreign markets, regulatory conditions in such markets, unanticipated changes in expenses or sales, changes in competitive conditions or other barriers to entry or expansion.

- The Company's belief as to future activities that may be undertaken to expand the Company's business--Actual activities undertaken may be impacted by general market conditions, competitive conditions in the Company's industry, unanticipated changes in the Company's financial position or the inability to identify attractive acquisition targets or other business opportunities.

CRITICAL ACCOUNTING POLICIES

The Company prepares the 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 policies, which IKONICS believes are the most critical to aid in fully understanding and evaluating its reported financial results, include the following:

Accounts Receivable. Trade receivables are carried at original invoice amount less an estimate made for doubtful receivables based on a review of all outstanding amounts on a monthly basis. Management determines the allowance for doubtful accounts by regularly evaluating individual customer receivables and considering a customer's financial condition, credit history, and current economic conditions. Trade receivables are written off when deemed uncollectible. Recoveries of trade receivables previously written off are recorded when received.

A trade receivable is considered to be past due if any portion of the receivable balance is outstanding for more than 90 days. While 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. The general payment terms are net 30-45 days for domestic customers and net 60-90 days for foreign customers. The concentration of credit risk is not significant except for a receivable from one of the Company's larger customers, which accounted for 9.5% of total receivables as of June 30, 2003.

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

Deferred Tax Assets. At June 30, 2003, the Company had approximately $200,000 of net deferred tax assets. The deferred tax assets result primarily due to timing differences in intangible assets and property and equipment. The Company has recorded a $50,000 valuation allowance to reserve for capital loss carryforwards that will more likely than not be realized. The Company has determined that it is more likely than not that the remaining deferred tax assets will be realized and that an additional valuation allowance for such assets is not currently required.

Revenue Recognition. The Company recognizes revenue on products when title passes, which is usually upon shipment. Freight billed to customers is included in sales. Shipping costs are included in cost of goods sold.

RESULTS OF OPERATIONS

QUARTER ENDED JUNE 30, 2003 COMPARED TO QUARTER ENDED JUNE 30, 2002

Sales. The Company's sales during the second quarter of 2003 were $3.16 million, which was essentially flat with the sales in the second quarter of 2002. Sales were higher domestically and in Europe offset by lower sales to Asia. A container shipment previously scheduled for China in the second quarter is now scheduled to be shipped and will be recorded in the third quarter of 2003.

Cost of Goods Sold. Cost of goods sold during the second quarter of 2003 was $1.69 million, or 53.4% of sales, compared to $1.77 million, or 56.0% of sales, during the same period in 2002. The reduction in the cost of sales in the first quarter of 2003 as a percentage of sales reflects an improved product mix across all geographic areas and lower costs for some of the raw materials. The Company also ended sales to certain marginally profitable customers at the beginning of the year.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased to $1,050,000, or 33.2% of sales, in the second quarter of 2003, from $1,015,000, or 32.1% of sales, for the same period in 2002. The second quarter of 2003 reflected higher sales and marketing expenses including costs to set up a training facility in Singapore and other trade show costs.

Loss on Investment. The Company wrote down the value of its investment in Apprise Technologies ("Apprise") by $75,000 in the second quarter of 2003. The latest offering price for shares of Apprise was below the value carried on the Company's books.

Research and Development Expenses. Research and development expenses during the second quarter of 2003 were $175,000, or 5.5% of sales, versus $187,000, or 5.9% of sales, for the same period in 2002. The reduction was due to lower costs for production trials and patent-related legal fees.

Interest Income. Interest income for the second quarter of 2003 was $3,000 compared to $10,000 for the same period in 2002. Interest is earned primarily from government obligation revenue bonds of various municipalities and school districts in the State of Minnesota.

Income Taxes. Income taxes were $19,000, or an effective rate of 12%, for the second quarter of 2003, versus income taxes of $69,000, or an effective rate of 35%, for the first quarter of 2002. The lower effective tax rate during the second quarter of 2003 relates to an increase in tax benefits of the extraterritorial income exclusion on foreign sales in prior years.

SIX MONTHS ENDED JUNE 30, 2003 COMPARED TO THE SIX MONTHS ENDED JUNE 30, 2002

Sales. The Company's sales during the first six months of 2003 increased moderately to $5.99 million, or less than 1.0%, from $5.95 million in sales during the same period in 2002. Domestic sales and European sales were higher but were offset by lower sales to Asia. A container shipment to China scheduled for the second quarter of 2003 is now scheduled to be shipped and will be recorded in the third quarter of 2003.

Cost of Goods Sold. Cost of goods sold during the first half of 2003 was $3.31 million, or 55.3% of sales, compared to $3.39 million, or 57.1% of sales, during the same period in 2002. The reduction in the cost of sales in the first six months of 2003 as a percentage of sales reflects an improved product mix across all geographic areas and lower costs for some raw materials. The Company also ended sales to certain marginally profitable customers at the beginning of the year.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased to $2,054,000, or 35.5% of sales, in the first half of 2003, from $1,966,000, or 33.1% of sales, for the same period in 2002. The first half of 2003 reflected higher sales and marketing expenses including costs to set up a training facility in Singapore, trade show costs and consulting. The Company also experienced higher public reporting costs related to new SEC regulations arising out of the Sarbanes-Oxley Act of 2002.

Loss on Investment. The Company wrote down the value of its investment in Apprise by $75,000. The latest offering price for shares of Apprise was below the value carried on the Company's books.

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Research and Development Expenses. Research and development expenses during the first half of 2003 were $343,000, or 5.7% of sales, versus $367,000, or 6.2% of sales, for the same period in 2002. The reduction was due to lower costs for production trials and patent-related legal fees.

Interest Income. Interest income was $16,000 for the first half of 2003 compared to $18,000 for the same period in 2002. Interest is earned primarily from government obligation revenue bonds of various municipalities and school districts in the State of Minnesota.

Income Taxes. Income taxes were $35,000, or an effective rate of 16%, for the first half of 2003 compared to $83,000, or an effective rate of 35%, for the first half of 2002.

LIQUIDITY AND CAPITAL RESOURCES

The Company has financed its operations principally with funds generated from operations. These funds have been sufficient to cover the Company's normal operating expenditures, annual capital requirements, and research and development expenditures.

Cash and cash equivalents were $822,000 and $210,000 at June 30, 2003 and June 30, 2002, respectively. The Company generated $557,000 in cash from operating activities during the three months ended June 30, 2003 and used $263,000 in cash from operating activities during the same period in 2002. Cash provided by operating activities is primarily the result of adjusting net income for non-cash depreciation, amortization, loss on investment provision for doubtful accounts, and certain changes in working capital components.

During the first six months of 2003, trade receivables increased by $180,000. The increase in receivables was driven by moderately higher sales and a temporary slowdown in domestic screen print customer payments due to economic conditions. The Company believes that the quality of its receivables is high and that strong internal controls are in place to maintain proper collections. The allowance for doubtful accounts was increased by $50,000 during the period to reflect the increase in trade receivables and the aging of these accounts related to the economic condition of the screen printing industry. Inventory levels increased by $152,000 reflecting increased stocks of AccuArt related products due to strong market acceptance. Accounts payable increased by $288,000, reflecting timing of payments for inventory to suppliers.

The Company used $119,000 and $148,000, in cash for investing activities during the six months ended June 30, 2003 and June 30, 2002, respectively. During the first six months of 2003, the Company purchased $92,000 in plant equipment upgrades to improve efficiency and reduce operating costs, additions to the Company's business software, improvements to the Company's trade show booths and construction costs on the leased training facility in Singapore. It also incurred $27,000 in patent application costs that the Company records as an asset and amortizes upon successful completion of the application process. During the first six months of 2002, the Company purchased $94,000 in capital equipment and business software. During the first half of 2002, the Company purchased, for $50,000, a license for technology applicable to its abrasive etching business.

Plans for additional capital expenditures of $100,000 during 2003 include ongoing manufacturing equipment upgrades, development equipment to modernize the capabilities and processes of the Company's research and development laboratory to improve measurement and quality control processes. Total 2003 planned expenditures are expected to be less than 2002 capital expenditures and are expected to be funded with cash generated from operating activities.

During the first quarter of 2002, the Company repurchased 23,500 shares of its outstanding Common Stock for $72,000.

A bank line of credit exists providing for borrowings of up to $1,250,000. Outstanding debt under this line of credit is collateralized by accounts receivable and inventory and bears interest at 2.25 percentage points over the 30-day LIBOR rate. The Company did not utilize this line of credit during the quarter ended June 30, 2003 and there was no debt outstanding under this line as of June 30, 2003. The Company made a $150,000 draw on this line of credit on June 20, 2002, primarily to cover a royalty payment to Aicello. The Company repaid this draw within a short period of time, utilizing cash from operations.

The Company believes that current financial resources, its line of credit, cash generated from operations and the Company's capacity for debt and/or equity financing will be sufficient to fund current and anticipated business operations. The Company also believes that its low debt levels and available line of credit make it unlikely that a decrease in demand for the Company's products would impair the Company's ability to fund operations.

INTERNATIONAL ACTIVITY

The Company markets its products to over 60 countries in North America, Europe, Latin America, Asia and other parts of the world. Foreign sales were approximately 30% of total sales for the three months ended June 30, 2003 and 31% of total sales for the three months ended June 30, 2002. Sales to foreign markets were 30% for the six months ended June 30, 2003 and 32% for the same period in 2002. Foreign sales in 2002 reflected higher sales to India and China. Fluctuations of certain foreign currencies have not significantly impacted the Company's operations because the Company's foreign sales are not concentrated in any one region of the world and are made primarily in dollars and Eurodollars. The Company believes its vulnerability to uncertainties due to foreign currency fluctuations and general economic conditions in foreign countries is not significant.

Substantially all of the Company's foreign transactions are negotiated, invoiced and paid in U.S. dollars or Eurodollars. IKONICS has not implemented a hedging strategy to reduce the risk of foreign currency translation exposures, which management does not believe to be significant based on the scope and geographic diversity of the Company's foreign operations as of June 30, 2003.

FUTURE OUTLOOK

IKONICS has invested over 6% of its sales dollars for the past several years in research and development. The Company plans to maintain its efforts in this area and expedite internal product development as well as form technological alliances with outside experts to ensure commercialization of new product opportunities.

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. In June, the Company opened a training center in Singapore.

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

ITEM 3. 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 controls 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 recorded, processed, summarized and reported within the time periods specified in SEC rules and forms. There was no change in the Company's internal control over financial reporting during the Company's most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting. However, the Company has found that certain internal control procedures were not being performed in a timely manner. When these deficiencies were discovered by supervising personnel, corrective actions were taken by the Company.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None

ITEM 2. CHANGES IN SECURITIES

None

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Company's Annual Meeting was held April 24, 2003. The shareholders took the following action:

The shareholders elected six directors to hold office until the next annual meeting of shareholders. The shareholders present in person or by proxy cast the following numbers of votes in connection with the election of directors, resulting in the election of all nominees:

	Votes For	Votes Against
Charles H. Andresen	1,064,696	42,765
David O. Harris	1,064,696	42,765
Gerald W. Simonson	1,064,696	42,765
William C. Ulland	1,064,696	42,765
Rondi Erickson	1,064,696	42,765
H. Leigh Severance	1,064,696	42,765

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) EXHIBITS

The following exhibits are filed as part of this Quarterly Report on Form 10-QSB for the quarterly period ended June 30, 2003:

Exhibit	Description
3.1	Restated Articles of Incorporation of Company, as amended.(1)
3.2	By-Laws of the Company, as amended.(1)
11	Computation of Net Earnings per Common Share.
31	Certifications pursuant to Rule 13a-14(a) of the Exchange Act.
32	Certifications pursuant to Rule 13a-14(b) of the Exchange Act.

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(1) Incorporated by reference to the like numbered Exhibit to the Company's Registration Statement on Form 10-SB (File No. 000-25727).

Copies of Exhibits will be furnished upon request and payment of the Company's reasonable expenses in furnishing the Exhibits.

(b) REPORTS ON FORM 8-K

On April 30, 2003, the Company filed a Current Report on Form 8-K including a press release announcing the Company's financial results for the three months ended March 31, 2003.

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: August 14, 2003

By: /s/ William C. Ulland
William C. Ulland,
Acting Chief Financial Officer,
Chairman, Chief Executive Officer,
and President

INDEX TO EXHIBITS

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31	Certifications pursuant to Rule 13a-14(a) of the Exchange Act.......	Filed Electron
32	Certifications pursuant to Rule 13a-14(b) of the Exchange Act.......	Filed Electron