ANNUAL REPORT

IKONICS Corporation

NASDAQ | IKNX

2014

CONTENTS

CORPORATE PROFILE

2014 Net Sales....$18,489,837
2014 Earnings per common share (diluted)....$0.32
Company founded....1952
Employees....75
NASDAQ Symbol....IKNX

COMPANY OVERVIEW

IKONICS is a corporation with four important technology platforms: Ultraviolet (UV) chemistry, film coating and construction, industrial inkjet printing and technical abrasive etching. IKONICS combines these technologies in various ways to create products and services for screen printers, manufacturers of awards and trophies, manufacturers of textured molds for plastic injection, and the custom machining of advanced composite materials and electronic wafers.

IKONICS' customer base includes over 25,000 end-users of its screen printing and awards and trophy products, suppliers to the worldwide automotive industry, and major civilian and military electronics and aerospace companies. IKONICS' products and services are used to manufacture products that range from T-shirts to the latest automobiles to the most advanced commercial and military aircraft.

IKONICS' key technologies are developed internally, and IKONICS believes it has a strong patent and trade secret position. All manufacturing is done in Duluth.

IKONICS believes this range of technologies and markets, and its strong financial condition, make IKONICS a very robust company that is buffered against many vagaries of the market and the economy. IKONICS' commitment to a range of new technologies gives it substantial growth potential.

Letter to Shareholders

The past year saw two of our new initiatives continue to gain momentum and position themselves for future growth. For the year, IKONICS Corporation experienced record sales of $18,500,000, a 6% percent increase over 2013. Earnings were down 5% from 2013 to $649,000, or $0.32 per diluted share.

Fourth quarter sales for our two new businesses – DTX, which works primarily with the automotive industry, and Advanced Materials Solutions (AMS), which serves the aerospace and electronics industries, were strong compared to the same quarter in 2013, and I believe sales for these businesses will continue to grow.

Our traditional Domestic screen print chemical business performed well for the year, helped by a partial return of manufacturing from China to the U.S. Our Export business was hurt by the same reshoring and the strength of the U.S. dollar, resulting in both declining sales and margins. I anticipate the strong dollar and weakening Asian markets to continue to impact our export sales in 2015.

In 2014, our IKONICS Imaging business unit had a very large film stocking order resulting in a 21% increase in IKONICS Imaging sales for the year. Although this remains a profitable and robust business, I do not expect a similar large stocking order in 2015.

AMS incurred increasing expenses in 2014 as we geared up to meet anticipated orders. Beginning in 2015, these orders have finally begun to arrive, and we now have three orders in house which I believe will be multiyear commitments. Additional orders are pending. These orders can always be canceled, but being chosen as a supplier at the beginning of a program often leads to being a supplier for the life of the program. Some of these programs have a life expectancy of more than 20 years. I believe in 2015 we will see accelerating growth in sales with profits beginning in 2016. Our AMS electronic wafer business also continues to grow.

In the 4th quarter of 2014, our DTX business, which supplies texturing and prototyping technology primarily to the automotive industry, turned its first profit with a sales increase of 132% over the same quarter of 2013. Although there may be some bumps in that growth rate, we are seeing broader market acceptance of this technology and are both selling system consumables and printing transfer and prototype film in-house and selling them worldwide.

I believe that our strategic plan to gain new markets through creative combinations of our core technology platforms of ultraviolet photochemistry, film coating and construction, technical abrasive etching, and industrial inkjet printing is beginning to pay off and will make IKONICS a unique and profitable technology company in the years ahead.

WILLIAM C. ULLAND

Chairman, President & CEO March 24, 2015

Special note regarding forward-looking statements

This 2014 Annual Report contains forward looking statements within the meaning of the safe harbor provisions of Section 21E of the Securities Exchange Act of 1934, as amended, relating to future events or the future financial performance of the Company. In some cases, you can identify forward-looking statements by the following words: "anticipate," "believe," "continue," "could," "estimate," "expect," "intend," "may," "ongoing," "plan," "potential," "predict," "project," "should," "will," "would," or the negative of these terms or other comparable terminology, although not all forward-looking statements contain these words. Forward looking statements are only predictions or statements of intention subject to risks and uncertainties and actual events or results could differ materially from those projected. Forward-looking statements are based on information available at the time the statements are made and involve known and unknown risks, uncertainties and other factors that may cause our results, levels of activity, performance or achievements to be materially different from the information expressed or implied by the forward-looking statements in this 2014 Annual Report. Factors that could cause actual results to differ include the risks, uncertainties and other matters set forth below under the caption "Risk Factors" and the matters set forth under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations," as well as those discussed in the Company's filings with the Securities and Exchange Commission.

Risk factors

The Company's DTX and AMS initiatives involve new technologies that might not be executed successfully and might not achieve market acceptance, which would adversely affect the Company's results of operation, financial condition and prospects.

The Company's DTX and AMS initiatives involve new and unproven technologies that might never achieve market acceptance. During 2014 and 2013, the Company generated operating losses in both its DTX and AMS segments. The Company's ability for generating profits from these initiatives will depend on its products gaining market acceptance among customers, which cannot be guaranteed. The degree of market acceptance of any new products the Company develops will depend on a number of factors, including:

- the Company's ability to successfully develop its technologies and products to include the capabilities the Company intends;

- the Company's ability to accurately assess the functions and features customers desire;

- the perceived effectiveness and price of the Company's products compared to alternative products and technologies;

- the development of new products and technologies by current competitors or new competitors that might enter the Company's markets; and

- the strength of the Company's marketing and distribution functions.

If new products that the Company develops do not have the capabilities the Company expects or fail to achieve an adequate level of acceptance by customers for any reason, then the Company's Micro-Machining and DTX business units could fail to generate the revenues the Company expects and may not become profitable or sustain profitability.

If the Company's new products and technologies do not achieve market acceptance, the Company will not realize a return on its investments in its new business initiatives.

The Company has invested, and plans to continue to invest, significant resources in its research and development efforts to develop technology for its AMS and DTX business units. The Company spent 3.6% of sales, or $665,000, on research and development in 2014 and 3.7% of sales, or $649,000, in 2013. A substantial portion of these investments was in the Company's AMS and DTX initiatives. The Company plans to continue to invest significant resources in research and development on these initiatives in the foreseeable future. The Company believes successful execution of these initiatives is important for its ability to grow its revenues and profits. However, if the Company fails to generate its projected revenues in these business units, the Company's investments in these areas would not generate the profits the Company expects and its results of operations, financial condition and prospects would be materially and adversely affected.

Adverse changes to global economic conditions generally, and to the aerospace and automotive industries in particular, may harm the Company's business.

The prospects for economic growth in the United States and other countries remain uncertain and major economies where the Company conducts business could continue or return to recessionary conditions. Economic concerns and issues such as reduced access to capital for businesses may cause the Company's customers to delay or reduce purchases of the Company's products. Given the continued uncertainty concerning the global economy, the Company also faces risks that may arise from financial difficulties experienced by suppliers and customers, such as an inability to collect receivables or the continued operation of suppliers.

The Company's AMS segment focuses primarily on customers in the aerospace industry, and its DTX segment focuses primarily on customers in the automotive industry. The aerospace and automotive industries have experienced volatility in recent years in a manner similar to or greater than the global economy generally. If either or both these industries experiences difficulties that reduce demand for their products generally, the Company's results of operations, financial condition and prospects would suffer.

The Company faces risks related to sales to government subcontractors, including potential delays or cancellations of planned sales and additional regulatory compliance costs and obligations.

The Company's customers for its AMS business unit manufacture aerospace products, and the Company derives a portion of its revenue as a subcontractor to general contractors working for the U.S. government. As a government subcontractor, demand and payment for the Company's products may be adversely affected by public sector budgetary cycles or funding authorizations. Any cancellation or delay of product orders would adversely affect the Company's operating results and financial condition.

In addition, government subcontractors are subject to oversight, including special rules on accounting, expenses, reviews and security. This additional oversight could increase the Company's compliance costs and creates risk of a failure to comply with applicable rules and regulations. A failure to comply with these rules and regulations could result in termination of contracts, fines and suspensions, debarment from future government business or other penalties, any of which could adversely affect the Company's business.

The Company faces significant competition and expects to face increasing competition in many aspects of its businesses, which could cause operating results to suffer.

The Company operates in highly competitive industries that experience rapid technological and market developments, changes in customer needs, and frequent product introductions and improvements, particularly with respect to the AMS and DTX businesses. If the Company is unable to anticipate and respond to these developments, its products or technologies could become uncompetitive or obsolete. Most of the Company's competitors in the AMS and DTX fields are larger and better capitalized than the Company with longer operating histories. These advantages could allow the Company's competitors to invest more in research and development and sales and marketing than the Company, which could make the competitive products more attractive or better known to consumers than the Company's products. In addition, because there is rapid technological change in fields in which the Company operates, the Company could face competition from new sources in the future that customers find more attractive.

The Company also could face increased competition in its traditional Domestic and IKONICS Imaging units. Capital costs for machinery necessary to operate in these industries have decreased in recent years, increasing the possibility that the Company will face new competitors. An increase in the amount of competition the Company faces, or a loss of competitiveness in any of the Company's business units for any reason, could adversely affect its revenues and gross margins.

The Company's failure to comply with environmental laws and regulations could harm its business and results of operations.

The manufacturing of the Company's products requires the use of hazardous materials that are subject to a broad array of environmental laws and regulations. The Company's failure to comply with these laws or regulations could result in:

•regulatory penalties, fines and legal liabilities;

•suspension of production;

•alteration of manufacturing processes; and

•restrictions on the Company's operations or sales.

The Company's failure to manage the use, transportation, emissions, discharge, storage, recycling or disposal of hazardous materials could lead to increased costs or future liabilities. Environmental laws and regulations also could require the Company to acquire pollution abatement or remediation equipment, modify product designs or incur other expenses.

Third parties may claim the Company infringes their intellectual property rights, which could harm the Company's business.

The Company may face claims that it infringes other parties' intellectual rights. Regardless of a claim's merit, claims that the Company's products or processes infringe the intellectual property rights of others could cause the Company to incur large costs to respond to, defend, and resolve the claims, and they may divert the efforts and attention of management and technical personnel. As a result of any intellectual property rights infringement claims, the Company could be required to:

•pay infringement claims;

•stop manufacturing, using, or selling products or technology subject to infringement claims;

•develop other products or technology not subject to infringement claims, which could be time-consuming, costly or impossible; or

•license technology from the party claiming infringement, which license may not be available on commercially reasonable terms or at all.

These actions could harm the Company's competitive position, result in additional expenses, or require the Company to impair its assets. If the Company alters or stops production of affected items, its revenue could be harmed.

The Company may be unable to enforce or protect its intellectual property rights, which may harm its ability to compete and may harm its business.

The Company's ability to enforce its patents, trademarks and other intellectual property rights is subject to general litigation risks, as well as uncertainty as to the enforceability of the Company's intellectual property rights in various countries. If the Company seeks to enforce its rights, it could become subject to claims that its intellectual property rights are invalid, not enforceable, or licensed to the opposing party. The Company's assertion of intellectual property rights also could result in the other party seeking to assert claims against the Company, which could harm the Company's business. The Company's inability to enforce its intellectual property rights for any reason could harm its competitive position and business.

If the Company is unable to protect the confidentiality of its proprietary information and know-how, the value of its technology could be adversely affected.

In addition to patented technology, the Company relies on unpatented proprietary technology, trade secrets, processes and know-how. The Company generally seeks to protect this information by confidentiality agreements with employees, consultants, advisors and third parties. These agreements may be breached, and the Company may not have adequate remedies for any such breach. In addition, the Company's trade secrets may otherwise become known or be independently developed by competitors. To the extent that the Company's employees, consultants or contractors use intellectual property owned by others in their work for the Company, disputes may arise as to the rights in related or resulting know-how and inventions.

The Company operates a global business that exposes it to additional risks.

The Company operates throughout the world, including in the United States, Europe and China. These international operations create a variety of risks and uncertainties, including:

•rapid changes in government, economic and political policies and conditions, political or civil unrest or instability, terrorism or epidemics,

•fluctuations in foreign currency exchange rates;

•compliance with and changes in foreign laws and regulations, as well as U.S. laws affecting the activities of U.S. companies abroad, including the Foreign Corrupt Practices Act of 1977 (the "FCPA"), as amended;

•different, complex and changing laws governing intellectual property rights, sometimes affording companies lesser protection in certain areas;

•longer accounts receivable payment cycles and difficulties in collecting accounts receivable;

•protectionist laws and business practices that favor local producers; and

•potentially adverse tax consequences, including the complexities of foreign value added tax systems and restrictions on the repatriation of earnings.

The occurrence of any one of these risks could negatively affect the Company's international business and, consequently, its results of operations generally.

The Company faces risks related to sales through distributors and other third parties.

During 2014, approximately 73% of the Company's sales, including nearly all sales of its Domestic products and nearly all of its International sales, were conducted through third parties. Using third parties for distribution exposes the Company to many risks, including competitive pressure, concentration, credit risk and compliance risks. Distributors may sell products that compete with the Company's products, and the loss of a distributor could reduce the Company's revenue. Distributors may face financial difficulties, including bankruptcy, which could harm the Company's collection of accounts receivable and financial results. Violations of the FCPA or similar laws by distributors or other third-party intermediaries could have a material impact on the Company's business. Failing to manage risks related to the Company's use of distributors may reduce sales, increase expenses, and weaken its competitive position.

Increases in prices and declines in the availability of raw materials could negatively impact the Company's financial results.

Certain raw materials needed to manufacture products are obtained from a limited number of suppliers and many of the raw materials are petroleum-based. Under normal market conditions, these raw materials are generally available on the open market from a variety of producers. While alternate supplies of most key raw materials are available, supplier production outages may lead to strained supply-demand situations for certain raw materials. The substitution of key raw materials could require the Company to identify new supply sources, or reformulate and retest products or processes. From time to time, the prices and availability of these raw materials may fluctuate, which could impair the Company's ability to procure necessary materials, or increase the cost of manufacturing products. If the prices of raw materials increase in a short period of time, the Company may be unable to pass these increases on to its customers in a timely manner or at all, which could reduce its gross margins. Like most companies in the Company's industries, the Company does not have long-term supply contracts for most of its key raw materials, which exacerbates the foregoing risks to the Company.

If any of the Company's present single or limited source suppliers become unavailable or inadequate, its customer relationships, results of operations and financial condition may be adversely affected.

The Company acquires certain of its materials that are critical to its operations from a limited number of third parties. Should any of the Company's current single or limited source suppliers become unavailable or inadequate, or impose terms unacceptable to the Company such as increased pricing terms, the Company could be required to spend a significant amount of time and expense to develop alternate sources of supply, and may not be successful in doing so on acceptable terms or at all. If the Company is unable to find a suitable supplier for a particular material, it could be required to modify its existing business processes or offerings to accommodate the situation. As a result, the loss of a single or limited source supplier could adversely affect the Company's relationship with its customers and its results of operations and financial condition.

The Company depends on one manufacturer to make and sell DTX printers. If the manufacturer ceased to make or sell DTX printers, or failed to meet quality standards, the Company's financial results and prospects would be adversely affected.

The Company relies on one company to manufacture and sell DTX printers. If the manufacturer ceased to produce or devote resources to selling DTX printers, due to a change in company strategy, to focus on alternative initiatives, or for any other reason, the Company would need to find an alternative manufacturer and seller of DTX printers. Finding an alternative manufacturer and seller of DTX printers could result in additional costs and delays in growing the Company's DTX business unit, which would adversely affect the Company's financial results and prospects.

In addition, if these manufacturers failed to produce DTX printers that satisfy the Company's quality standards, the Company's reputation with end users could be harmed and the Company could be forced to find a new manufacturer. Either of these results also would harm the Company's business and prospects.

The inability to attract and retain qualified personnel could adversely impact the Company's business.

Sustaining and growing the Company's business depends on the recruitment, development and retention of qualified employees, including management and research and development personnel. The inability to recruit and retain key personnel or the unexpected loss of key personnel may adversely affect the Company's operations.

An active trading market for the Company's shares of common stock may not develop.

The Company's common stock has been listed for trading on the Nasdaq Capital Market since 1999 and persistently has experienced limited trading volume. There can be no assurance that an active public market for the Company's shares will develop or be sustained. The lack of an active trading market could adversely affect the price and liquidity of the Company's common stock.

The Company's directors and officers own a large percentage of the Company's common stock, which may allow them to collectively exert significant influence over substantially all matters requiring shareholder approval.

As of December 31, 2014, the Company's directors and officers collectively beneficially owned approximately 33.77% of its common stock outstanding as of that date. As a result, the Company's directors and officers could exert significant influence over all matters requiring a shareholder vote, including the election of directors, amendments to the Company's articles of incorporation, and extraordinary transactions such as mergers or going private transactions. These ownership positions may have the effect of delaying, deterring or preventing a change in control or a change in the composition of the Company's board of directors. In addition, substantial sales of shares beneficially owned by our directors or officers could be viewed negatively by third parties and have a negative impact on the Company's stock price.

The price of the Company's common stock may fluctuate significantly.

The price of the Company's common stock has, and could continue to, fluctuate substantially in a short period of time. The price of the Company's common stock could vary for many reasons, including the following:

- future announcements concerning the Company or its competitors;
- introduction of new products by the Company or its competitors, or the failure of the Company's new products to meet expectations;
- the commencement of, or developments to, litigation involving the Company;
- quarterly variations in operating results, which the Company has experienced in the past and expects to experience in the future;
- business acquisitions or divestitures; or
- changes to the global economy in general, and the aerospace and automotive markets in particular.

In addition, stock markets in general have experienced price and volume fluctuations in recent years, fluctuations that sometimes have been unrelated to the operating performance of the affected companies. These broad market fluctuations may adversely affect the market price of the Company's common stock. The market price of the Company's common stock could decline below its current price and the market price of the Company's shares may fluctuate significantly in the future. These fluctuations may be unrelated to the Company's performance.

The Company's operating results and financial condition may fluctuate on a quarterly and annual basis.

The Company's operating results and financial condition may fluctuate from quarter to quarter and year to year, and could vary due to a number of factors, some of which are outside of the Company's control. In addition, the Company's actual or projected operating results may fail to match its past performance. The Company's operating results and financial condition may fluctuate due to a number of factors, including those listed below and those identified throughout this "Risk Factors" section:

•the failure of the Company's new products to meet expectations;

•changes to the costs of raw materials, especially petroleum-based materials;

•the entry of new competitors into the Company's markets whether by established companies or by new companies;

•the geographic distribution of the Company's sales;

•changes in customer preferences or needs;

•changes in the amount that the Company invests to develop or acquire new technologies;

•delays between the Company's expenditures to develop new technologies and products and the generation of sales related thereto;

•changes in the Company's pricing policies or those of its competitors;

•changes in accounting rules and tax and other laws; and

•general economic and industry conditions that affect customer demand and product development trends.

Due to all of the foregoing factors and the other risks discussed in this "Risk Factors" section, you should not rely on quarter-to-quarter or year-to-year comparisons of the Company's operating results as an indicator of future performance.

Management's discussion and analysis of financial condition and results of operations

The following management discussion and analysis focuses on those factors that had a material effect on the Company's financial results of operations and financial condition during 2014 and 2013 and should be read in connection with the Company's audited financial statements and notes thereto for the years ended December 31, 2014 and 2013, included herein.

Critical accounting policies and 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 policies and estimates which IKONICS 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. 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 based on upon historical experience and any specifically identified issues for any customer related returns, refunds or credits.

Inventories – 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 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. 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 – The Company recognizes revenue on sales of products when title passes which can occur at the time of shipment or when the goods arrive at the customer location depending on the agreement with the customer. The Company sells its products to both distributors and end-users. Sales to distributors and end-users are recorded based upon the criteria governed by the sales, delivery, and payment terms stated on the invoices from the Company to the purchaser. In addition to transfer of title / risk of loss, all revenue is recorded in accordance with the criteria outlined within SAB 104 and FASB ASC 605 Revenue Recognition:

a.) persuasive evidence of an arrangement (principally in the form of customer sales orders and the Company's sales invoices)

b.) delivery and performance (evidenced by proof of delivery, e.g. the shipment of film and substrates with bill of lading used for proof of delivery for FOB shipping point terms, and the carrier booking confirmation report used for FOB destination terms). Once the finished product is shipped and physically delivered under the terms of the invoice and sales order, the Company has no additional performance or service obligations to complete

c.) a fixed and determinable sales price (the Company's pricing is established and is not based on variable terms, as evidenced in either the Company's invoices or the limited number of distribution agreements; the Company rarely grants extended payment terms and has no history of concessions)

d.) a reasonable likelihood of payment (the Company's terms are standard, and the Company does not have a substantial history of customer defaults or non-payment)

Sales are reported on a net basis by deducting credits, estimated normal returns and discounts. The Company's return policy does not vary by geography. The customer has no rotation or price protection rights and the Company is not under a warranty obligation. Freight billed to customers is included in sales. Shipping costs are included in cost of goods sold.

Results of operations

YEAR ENDED DECEMBER 31, 2014 COMPARED TO YEAR ENDED DECEMBER 31, 2013

Sales – The Company's net sales increased 5.7% in 2014 to a record $18.5 million compared to net sales of $17.5 million in 2013. IKONICS Imaging sales grew $807,000, or 21.0%, to $4.6 million mainly due to a large initial stocking order from its new distributor, JDS Industries. The Company expects continued sales from JDS Industries, but not at the volume of the 2014 initial stocking order. IKONICS Imaging sales have also been positively impacted by improved equipment sales. Domestic sales increased 8.1% in 2014 due to improved emulsion sales as a result of increased customer demand for existing and newly introduced products into the Company's traditional markets. DTX sales also grew from $407,000 in 2013 to $423,000 in 2014 due to higher film sales. These sales increases were partially offset by a 6.9% Export sales decrease due to lower sales across all geographic regions. Asia and Europe realized the largest decreases in 2014 compared to the prior year due to poorer general economic conditions and a weaker Euro. Also unfavorably impacting sales in 2014 was a 5.3% decrease in AMS sales due to loss of a large mask customer.

Gross Profit – Gross profit in 2014 was $6.7 million, or 36.3% of sales, compared to $6.9 million, or 39.7% of sales in 2013. Gross margins were unfavorably impacted by an increase in AMS production costs related to the Company's efforts to improve its production capacity and capabilities. DTX costs also increased in 2014 as the Company allocated additional resources, both personnel and equipment, to produce textured prints. Some DTX resources used in the production of textured prints were previously utilized in a selling and administrative capacity. Domestic gross margins were negatively impacted by a less favorable sales mix as sales volumes for lower margin emulsion sales grew relative to higher margin film sales. The Export gross margin also declined from 28.1% in 2013 to 26.8% in 2014 due to both a stronger U.S. dollar and a less favorable sales mix. An increase in sales volumes and a more favorable sales mix improved the IKONICS Imaging gross margin in 2014 to 53.3% from 52.3% in 2013.

Selling, General and Administrative Expenses – Selling, general and administrative expenses were $5.1 million, or 27.7% of sales, in 2014 compared to $5.4 million, or 30.7% of sales, in 2013. The decrease reflects lower DTX selling, general and administrative expenses compared to the same period last year as internal resources, both personnel and equipment, previously involved with selling, general and administrative duties were reassigned to the production of textured prints in 2014. Selling, general and administrative expenses also benefitted from lower IKONICS Imaging and Export promotional expenses.

Research and Development Expenses – Research and development expenses in 2014 were $665,000, or 3.6% of sales, versus $649,000, or 3.7% of sales, in 2013. The increase is related to higher production trial and personnel expenses for the year, partially offset by lower depreciation expenses. The increase in production trial expenses was partially related to efforts to improve DTX consumable products to meet customer requirements.

Income Taxes – During 2014, the Company realized income tax expense of $270,000, or an effective rate of 29.4%, compared to income tax expense of $245,000, or an effective rate of 26.4%, for the same period in 2013. The increase in current year tax expense and effective rate from 2013 is primarily due to benefits from prior year adjustments recognized in 2013 as well as higher research and development credits generated in the prior year. The income tax provision for the 2014 and 2013 periods differs from the expected tax expense due to the benefits of the domestic manufacturing deduction, credits for research and development and other non-deductible items.

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, research and development expenditures.

Cash and cash equivalents were $1.9 million and $1.7 million at December 31, 2014 and 2013, respectively. In addition to its cash, the Company also held $1.8 million of short-term investments as of December 31, 2014 and $1.5 million of short-term investments as of December 31, 2013. The Company generated $917,000 in cash from operating activities during 2014, compared to generating $1.5 million of cash from operating activities in 2013. Cash provided by operating activities is primarily the result of the net income adjusted for non-cash depreciation and amortization, deferred taxes, and certain changes in working capital components discussed in the following paragraph.

During 2014, inventories increased by $76,000. In addition to increased finished goods levels, part of the inventory increase is related to the timing of raw material purchases. Trade receivables increased $45,000 related to the increase in sales volumes. The $17,000 decrease in prepaid expenses and other assets is related to a decrease in prepaid promotional expenses. Accounts payable decreased $161,000 due to the timing of payments to and purchases from vendors while accrued liabilities increased $31,000 due to the timing of the Company's payroll. The Company's income tax receivable increased $122,000 due to timing of estimated 2014 tax payments compared to the calculated 2014 tax liability.

During 2013, inventories decreased by $124,000. Lower raw material levels are related to the timing of purchases and efforts to tighten inventory volumes. The $21,000 decrease in prepaid expenses and other assets is related to timing of insurance payments while trade receivables decreased by $9,000. Accounts payable decreased $62,000 due to the timing of payments to and purchases from vendors while accrued liabilities decreased $5,000. Income taxes payable decreased $62,000 and income tax receivable increased $16,000 due to the timing of estimated 2013 tax payments compared to the calculated 2013 tax liability.

During 2014, investing activities used $731,000. Purchases of property and equipment were $434,000, mainly for improvements to AMS equipment, mandatory elevator upgrades, two forklifts and two vehicles. The Company realized $62,000 in proceeds from the sale of land and two vehicles. Also during 2014, the Company incurred $57,000 in patent application costs that the Company records as an asset and amortizes upon successful completion of the application process. The Company also invested $2.7 million in 18 fully insured certificates of deposit during 2014. Eighteen certificates of deposit totaling $2.4 million matured during 2014.

During 2013, investing activities used $820,000. Purchases of property and equipment were $763,000. The majority of these purchases were made to improve AMS capabilities. Equipment purchases were also made to upgrade research and development equipment and facilities, including improvements to both DTX equipment and equipment and facilities related to screen printing and IKONICS Imaging. The Company realized $36,000 in proceeds from the sale of two vehicles. Also in 2013, the Company incurred $71,000 in patent application costs that the Company records as an asset and amortizes upon successful completion of the application process. The Company also invested $1.8 million in 12 fully insured certificates of deposit during 2013. Twelve certificates of deposit totaling $1.8 million matured during 2013.

In 2014, the Company received $46,000 from financing activities from the issuance of 6,083 shares of common stock from the exercise of stock options compared to $89,000 the Company received from the issuance of 13,695 shares of common stock from the exercise of stock options in 2013.

A bank line of credit exists providing for borrowings of up to $1.25 million through May 31, 2015. The Company expects to renew this line of credit or obtain a similar line of credit when the current line of credit expires. The line of credit is collateralized by trade receivables and inventories and bears interest at 2.5 percentage points over the 30-day LIBOR rate. The Company did not utilize this line of credit during 2014 and 2013 and there were no borrowings outstanding as of December 31, 2014 and 2013. There are no financial covenants related to the line of credit.

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.

Capital expenditures

In 2014, the Company spent $434,000 on capital expenditures. Capital expenditures in 2014 were mainly for improvements to AMS capabilities, mandatory elevator upgrades, two forklifts and two vehicles.

During 2013, the Company had $763,000 of capital expenditures. The majority of these purchases were made to improve AMS capabilities. Equipment purchases were also made to upgrade research and development equipment and facilities, including improvements to both DTX equipment and equipment and facilities related to screen printing and IKONICS Imaging in addition to a vehicle for sales personnel.

The Company expects capital expenditures in 2015 of approximately $900,000. The planned expenditures primarily will be for mandatory elevator upgrades not completed in 2014, manufacturing equipment necessary for anticipated AMS aerospace business, other manufacturing equipment upgrades and vehicles for sales personnel. These commitments are expected to be funded with cash generated from operating activities. The Company is also beginning to plan and evaluate a potential building expansion to accommodate its AMS operations as the Company's current facilities are nearing full capacity. This expansion, along with the expected 2015 purchase of the AMS equipment mentioned above will be dependent on the Company's AMS process proving its capabilities and increasing its market acceptance among its customers base. The Company does not intend to proceed with the expansion until the demand for its services is more certain. The timing and cost of this expansion have not been finalized, but construction could commence in 2015. Any costs associated with this potential expansion are not included in the Company's estimated capital expenditures for 2015 discussed above.

International activity

The Company markets its products in numerous countries in various regions of the world, including North America, Europe, Latin America, and Asia. The Company's 2014 foreign sales of $5.3 million were approximately 28.4% of total sales, compared to the 2013 foreign sales of $5.6 million, which were 32.3% of total sales. IKONICS experienced a decrease in foreign sales across all geographic regions in 2014 due to due to poorer general economic conditions and a weaker Euro.

The Company's foreign transactions are primarily negotiated, invoiced and paid in U.S. dollars, while a portion is transacted in Euros. IKONICS has not implemented an economic 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 December 31, 2014. Furthermore, the impact of foreign exchange on the Company's balance sheet and operating results was not material in either 2014 or 2013.

Future outlook

IKONICS has spent on average approximately 4% of its sales dollars for the past few years in research and development and has made capital expenditures related to its DTX and AMS programs. The Company plans to maintain its efforts in this area to expedite internal product development as well as to form technological alliances with outside experts to commercialize new product opportunities.

The Company continues to make progress on its new AMS business initiative. The Company has entered into agreements with several major aerospace companies to determine the feasibility of using its unique technologies in the production of military and commercial aircraft. The Company is currently supplying products to the aerospace industry for use in the construction of new generation commercial aircraft. Progress is being made on a number of in-house feasibility projects, and the Company believes that several of these could lead to ongoing business. In anticipation of this business, the Company is expanding its AMS capacity and patent applications.

The Company is also continuing to make progress on its DTX business initiatives. In addition to its growing 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 with its DTX customers on training, production optimization, and product improvements. The Company has been awarded European, Japanese and United States patents on its DTX technologies. The Company has modified its DTX technology to enter the market for prototyping and 3D printing.

Domestically, both the Domestic Chromaline Screen Print Product and its IKONICS Imaging units remain profitable in mature markets and require aggressive strategies to grow market share. Although there will be challenges, the Company believes these businesses will continue to grow and prosper. 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.

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

Off-balance sheet arrangements

The Company has no off-balance sheet arrangements.

Recent accounting pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers. ASU 2014-09 supersedes the revenue recognition requirements in Revenue Recognition (Topic 605), and requires entities to recognize revenue in a way that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. ASU 2014-09 is effective for the Company in our fiscal year beginning on January 1, 2017, including interim periods within that reporting period and is to be applied retrospectively, with early application not permitted. The Company is currently evaluating the effect that adopting this new accounting guidance will have on our consolidated results of operations, cash flows and financial position.

In August 2014, FASB issued ASU No. 2014-15, 'Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern, intended to define management's responsibility to evaluate whether there is substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures. ASU 2014-15 is effective for the Company in the year ended December 31, 2016, and interim periods beginning March 31, 2017, with early application permitted. The Company does not anticipate a material impact to the financial statements once implemented.

Market for common equity and related stockholder matters

The Company's Common Stock is traded on the Nasdaq Capital Market under the symbol IKNX. The following table sets forth, for the fiscal quarters indicated, the high and low sales prices for the Company's Common Stock as reported on the Nasdaq Capital Market for the periods indicated.

Fiscal Year Ended December 31, 2014:	**High**	**Low**
First Quarter	$ 31.02	$ 13.50
Second Quarter	29.00	19.90
Third Quarter	27.20	17.06
Fourth Quarter	17.82	14.03

Fiscal Year Ended December 31, 2013:		
First Quarter	$ 13.74	$ 7.92
Second Quarter	17.99	12.00
Third Quarter	18.98	16.06
Fourth Quarter	19.45	14.25

As of February 19, 2015, the Company had approximately 699 shareholders. Declaration and payment of dividends is within the sole discretion of the Company's board of directors.

Management's report

The financial statements of IKONICS Corporation have been prepared by Company management who are responsible for their content. These statements have been prepared in accordance with accounting principles generally accepted in the United States of America and, where appropriate, reflect estimates based on judgements of management.

The financial statements have been audited by McGladrey LLP, an independent registered public accounting firm.

The Audit Committee of the Board of Directors, comprised of outside directors, meets periodically with the independent auditors and management to discuss the Company's internal accounting controls and financial reporting matters. Our independent registered public accounting firm has unrestricted access to the Audit Committee, without management present, to discuss the results of their audit, the adequacy of internal accounting controls, and the quality of financial reports.

WILLIAM C. ULLAND
Chairman, President & CEO

JON GERLACH
Chief Financial Officer & V.P. Finance

Management's annual report on internal control over financial reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Our internal control system is designed to provide reasonable assurance to our management and board of directors regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that:

- Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;

- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and

- Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Management assessed the effectiveness of our internal control over financial reporting as of December 31, 2014. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control – Integrated Framework. Based on management's assessment and those criteria, management believes that, as of December 31, 2014, the Company maintained effective internal control over financial reporting.

This annual report does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Our management's report of the effectiveness on the design and operation of our internal control over financial reporting was not subject to attestation by the Company's registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit the Company to provide only management's report in this annual report.

WILLIAM C. ULLAND
Chairman, President & CEO

JON GERLACH
Chief Financial Officer & V.P. Finance

Report of independent registered public accounting firm

TO THE BOARD OF DIRECTORS AND STOCKHOLDERS
IKONICS CORPORATION

We have audited the accompanying balance sheets of IKONICS Corporation as of December 31, 2014 and 2013, and the related statements of income, stockholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of IKONICS Corporation as of December 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

/s/ McGladrey LLP
Minneapolis, Minnesota
March 5, 2015

BALANCE SHEETS

DECEMBER 31, 2014 AND 2013

ASSETS		2014		2013
CURRENT ASSETS:				
Cash and cash equivalents (Note 7)	$	1,936,214	$	1,704,300
Short-term investments		1,766,000		1,464,878
Trade receivables, less allowance of $49,000 in 2014 and $62,000 in 2013 (Notes 5, 7, and 8)		2,096,328		2,050,853
Inventories (Note 8)		2,630,650		2,554,942
Prepaid expenses and other assets		86,400		103,687
Income tax receivable		163,651		16,400
Deferred income taxes (Note 2)		178,000		150,000
Total current assets		8,857,243		8,045,060
PROPERTY, PLANT, AND EQUIPMENT, AT COST:				
Land and building		6,247,781		6,123,890
Machinery and equipment		3,956,561		3,781,282
Office equipment		754,220		722,567
Vehicles		247,356		237,194
		11,205,918		10,864,933
Less accumulated depreciation		5,789,070		5,230,837
		5,416,848		5,634,096
INTANGIBLE ASSETS, less accumulated amortization of $198,918 in 2014 and $173,143 in 2013 (Note 3)		353,871		322,647
	$	14,627,962	$	14,001,803

LIABILITIES AND STOCKHOLDERS' EQUITY		2014		2013
CURRENT LIABILITIES:				
Accounts payable	$	371,181	$	532,294
Accrued compensation		294,706		274,936
Other accrued liabilities		78,610		67,755
Total current liabilities		744,497		874,985
DEFERRED INCOME TAXES (Note 2)		545,000		527,000
Total liabilities		1,289,497		1,401,985
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 2,018,253 shares in 2014 and 2,012,170 shares in 2013 (Note 6)		201,825		201,217
Additional paid-in capital		2,681,307		2,592,038
Retained earnings		10,455,333		9,806,563
Total stockholders' equity		13,338,465		12,599,818
	$	14,627,962	$	14,001,803

See notes to financial statements.

Statements of Income

YEARS ENDED DECEMBER 31, 2014 AND 2013

	2014	2013
NET SALES	$ 18,489,837	$ 17,491,408
COST OF GOODS SOLD	11,786,608	10,553,553
GROSS PROFIT	6,703,229	6,937,855
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	5,124,764	5,368,400
RESEARCH AND DEVELOPMENT EXPENSES	664,999	649,325
	5,789,763	6,017,725
INCOME FROM OPERATIONS	913,466	920,130
OTHER	5,304	7,043
INCOME BEFORE INCOME TAXES	918,770	927,173
FEDERAL AND STATE INCOME TAXES (NOTE 2)	270,000	245,000
NET INCOME	$ 648,770	$ 682,173
EARNINGS PER COMMON SHARE:		
Basic	$ 0.32	$ 0.34
Diluted	$ 0.32	$ 0.34
WEIGHTED AVERAGE COMMON SHARES:		
Basic	2,017,144	2,006,843
Diluted	2,018,334	2,010,659

See notes to financial statements.

Statements of stockholders' equity

YEARS ENDED DECEMBER 31, 2014 AND 2013

	Common Shares	Stock Amount	Additional Paid-In Capital	Retained Earnings	Total Stockholders' Equity
Balance At December 31, 2012	1,998,475	$ 199,848	$ 2,470,507	$ 9,124,390	$ 11,794,745
Net income	-	-	-	682,173	682,173
Exercise of stock options	13,695	1,369	88,029	-	89,398
Tax benefit resulting from stock option exercises	-	-	19,595	-	19,595
Stock based compensation and related tax benefit	-	-	13,907	-	13,907
Balance At December 31, 2013	2,012,170	201,217	2,592,038	9,806,563	12,599,818
Net income	-			648,770	648,770
Exercise of stock options	6,083	608	45,379	-	45,987
Tax benefit resulting from stock option exercises	-	-	25,475	-	25,475
Stock based compensation and related tax benefit	-	-	18,415	-	18,415
Balance At December 31, 2014	2,018,253	$ 201,825	$ 2,681,307	$ 10,455,333	$ 13,338,465

See notes to financial statements.

STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2014 AND 2013

	2014	2013
CASH FLOW FROM OPERATING ACTIVITIES:		
Net Income	$ 648,770	$ 682,173
ADJUSTMENTS TO RECONCILE NET INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Depreciation	635,607	568,791
Amortization	25,775	53,314
Stock based compensation	18,415	13,907
Net gain on disposal of property, plant and equipment	(45,659)	(13,979)
Deferred income taxes	(10,000)	153,000
CHANGES IN OPERATING ASSETS AND LIABILITIES		
Trade receivables	(45,475)	9,459
Inventories	(75,708)	123,922
Prepaid expenses and other assets	17,287	21,296
Income tax receivable	(121,776)	(16,400)
Accounts payable	(161,113)	(61,628)
Accrued liabilities	30,625	(4,766)
Income taxes payable	---	(62,557)
Net cash provided by operating activities	916,748	1,466,532
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(434,463)	(762,537)
Proceeds from disposal of property and equipment	61,763	35,507
Purchases of intangibles	(56,998)	(70,604)
Purchases of short-term investments	(2,716,000)	(1,814,878)
Proceeds from sale of short-term investments	2,414,877	1,792,939
Net cash used in investing activities	(730,821)	(819,573)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from exercise of stock options	45,987	89,398
NET INCREASE IN CASH AND CASH EQUIVALENTS	231,914	736,357
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	1,704,300	967,943
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 1,936,214	$ 1,704,300
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid for income taxes, net of taxes received of $13,026 in 2013	$ 401,776	$ 171,139

See notes to financial statements

Notes to financial statements

YEARS ENDED DECEMBER 31, 2014 AND 2013

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business and Foreign Export Sales - IKONICS Corporation's (the Company) traditional business has been the development and manufacturing of high-quality photochemical imaging systems for sale primarily to a wide range of printers and decorators of surfaces. Customers' applications are primarily screen printing and abrasive etching. These sales have been augmented with inkjet receptive films, ancillary chemicals and related equipment to provide a full line of products and services to its customers. In 2006, the Company began a major effort to diversify and expand its business to industrial markets. These efforts now include the Company's Advanced Material Solutions (AMS) business unit, formerly named Micro-Machining, which uses the Company's proprietary process and photoresist film for the abrasive etching of composite materials, industrial ceramics, silicon wafers, and glass wafers. The customer base for AMS is primarily the aerospace and electronics industries. Based on its expertise in ultraviolet curable fluids and inkjet receptive substrates, the Company has also developed a patented digital texturing technology (DTX) for putting patterns and textures into steel molds for the plastic injection molding industry. The ultimate original equipment manufacturer ("OEM") for the Company's DTX technology is primarily the automotive industry. The Company offers a suite of products to the mold making industry. Industrial inkjet printers, which are integral to the DTX system, are manufactured and sold by a strategic partner. The Company's business plan is to sell consumable fluids and transfer films. For most markets these sales are direct to the mold maker. The DTX technology is being expanded to prototyping where the Company's technology offers a unique combination of high definition and large format prints. The Company's principal markets are throughout the United States. In addition, the Company sells to Europe, Latin America, Asia, and other parts of the world. The Company extends credit to its customers, all on an unsecured basis, on terms that it establishes for individual customers.

Foreign export sales approximated 28.4% of net sales in 2014 and 32.3% of net sales in 2013. The Company's trade receivables at December 31, 2014 and 2013 due from foreign customers were 30.6% and 32.5% of total trade receivables, respectively. The foreign export receivables are composed primarily of open credit arrangements with terms ranging from 30 to 90 days. No single customer or foreign country represented greater than 10% of net sales in 2014 or in 2013.

The Company considers events or transactions that occur after the balance sheet date but before the financial statements are issued to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure.

A summary of the Company's significant accounting policies follows:

Cash Equivalents - The Company considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. Cash equivalents consist of money market funds in which the carrying value approximates market value because of the short maturity of these instruments. The money market fund utilized by IKONICS invests in United States dollar denominated securities that present minimal credit risk and consist of investments in debt securities issued or guaranteed by the United States government or by United States government agencies or instrumentalities and repurchase agreements fully collateralized by the United States Treasury and United States government securities.

Short-Term Investments - Short-term investments consist of fully insured certificates of deposit with original maturities ranging from four to twelve months as of December 31, 2014 and 2013, respectively.

Trade Receivables - Trade receivables are carried at original invoice amount less an estimate made for doubtful receivables based on a review of all outstanding amounts on an on-going 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. Accounts are considered past due if payment is not received according to agreed-upon terms.

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 Financial Accounting Standards Board ("FASB") Accounting Standard Codification ("ASC") No. 830, Foreign Currency Matters. Foreign currency transactions and translation adjustments did not have a significant effect on the Balance Sheet or the Statements of Income, Stockholders' Equity and Cash Flows for 2014 and 2013.

Inventories - Inventories are stated at the lower of cost or market using the last-in, first-out (LIFO) method. If the first-in, first-out (FIFO) cost method had been used, inventories would have been approximately $1,315,000 and $1,248,000 higher than reported at December 31, 2014 and 2013, respectively. The inventory reserve for obsolescence was $11,000 and $15,000 at December 31, 2014 and 2013, respectively. The major components of inventories are as follows:

		2014		2013
Raw Materials	$	2,020,151	$	1,952,398
Work-in-progress		407,964		389,501
Finished goods		1,517,151		1,461,264
Reduction to LIFO cost		(1,314,616)		(1,248,221)
Total Inventories	$	2,630,650	$	2,554,942

Property, Plant and Equipment - Major expenditures extending the life of the property, plant and equipment are capitalized. Repair and maintenance costs are expensed in the period in which they are incurred. Depreciation of property, plant and equipment is computed using the straight-line method over the following estimated useful lives:

	Years
Buildings	15-40
Machinery and equipment	5-10
Office equipment	3-10
Vehicles	3

Intangible Assets – Intangible assets consist of patents, licenses and covenants not to compete arising from business acquisitions. Intangible assets are amortized on a straight-line basis over their estimated useful lives or agreement terms. To the extent the undiscounted cash flows are less than the carrying value, analysis is performed based on several criteria, including, but not limited to, revenue trends, discounted operating cash flows and other operating factors to determine the impairment amount.

As of December 31, 2014, the remaining estimated weighted average useful lives of intangible assets are as follows:

	Years
Patents	13.4
Licenses	2.7
Non-compete agreements	0.5

Impairment of Long-lived Assets – The Company reviews its long-lived assets, including property, plant and equipment and intangible assets, for impairment when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amount. Any impairment loss recorded is measured as the amount by which the carrying value of the assets exceeds the fair value of the assets. To date, the Company has determined that no impairment of long-lived assets exists.

Fair Value of Financial Instruments – The carrying amounts of financial instruments, including cash and cash equivalents, short-term investments, trade receivables, accounts payable, and accrued liabilities approximate fair value due to the short maturities of these instruments.

Revenue Recognition - The Company recognizes revenue on sales of products when title passes which can occur at the time of shipment or when the goods arrive at the customer location depending on the agreement with the customer. The Company sells its products to both distributors and end-users. Sales to distributors and end-users are recorded based upon the criteria governed by the sales, delivery, and payment terms stated on the invoices from the Company to the purchaser. In addition to transfer of title / risk of loss, all revenue is recorded in accordance with the criteria outlined within SAB 104 and FASB ASC 605 Revenue Recognition:

(a) persuasive evidence of an arrangement (principally in the form of customer sales orders and the Company's sales invoices, as generally there is no other formal agreement underlying the sale transactions)

(b) delivery and performance (evidenced by proof of delivery, e.g. the shipment of film and substrates with bill of lading used for proof of delivery for FOB shipping point terms, and the carrier booking confirmation report used for FOB destination terms. Once the finished product is shipped and physically delivered under the terms of the invoice and sales order, the Company has no additional performance or service obligations to complete)

(c) a fixed and determinable sales price (the Company's pricing is established and is not based on variable terms, as evidenced in either the Company's invoices or the limited number of distribution agreements; the Company rarely grants extended payment terms and has no history of concessions)

(d) a reasonable likelihood of payment (the Company's terms are standard, and the Company does not have a substantial history of customer defaults or non-payment)

Sales are reported on a net basis by deducting credits, estimated normal returns and discounts. The Company's return policy does not vary by geography. The customer has no rotation or price protection rights and the Company is not under a warranty obligation. Freight billed to customers is included in sales. Shipping costs are included in cost of goods sold.

Deferred 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. 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.

Earnings per Common Share (EPS) - Basic EPS is calculated using net income divided by the weighted average of common shares outstanding. Diluted EPS is similar to Basic EPS except that the weighted average number of common shares outstanding is increased to include the number of additional common shares, when dilutive, that would have been outstanding if the potential dilutive common shares, such as those shares subject to options, had been issued.

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

	2014	2013
Weighted average common shares outstanding	2,017,144	2,006,843
Dilutive effect of stock options	1,190	3,816
Weighted average common and common equivalent shares outstanding	2,018,334	2,010,659

At December 31, 2014, options to purchase 1,250 shares of common stock with a weighted average exercise price of $28.25 were outstanding, but were excluded from the computation of common share equivalents because they were anti-dilutive. There were no anti-dilutive options at December 31, 2013.

Employee Stock Plan - The Company accounts for employee stock options under the provision of ASC 718 Compensation – Stock Compensation.

Recent Accounting Pronouncements - In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers. ASU 2014-09 supersedes the revenue recognition requirements in Revenue Recognition (Topic 605), and requires entities to recognize revenue in a way that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. ASU 2014-09 is effective for the Company in our fiscal year beginning on January 1, 2017, including interim periods within that reporting period and is to be applied retrospectively, with early application not permitted. The Company is currently evaluating the effect that adopting this new accounting guidance will have on our consolidated results of operations, cash flows and financial position.

In August 2014, FASB issued ASU No. 2014-15, Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern, intended to define management's responsibility to evaluate whether there is substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures. ASU 2014-15 is effective for the Company in the year ended December 31, 2016, and interim periods beginning March 31, 2017, with early application permitted. The Company does not anticipate a material impact to the financial statements once implemented.

Use of Estimates - The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates include the allowance for doubtful trade receivables, the reserve for inventory obsolescence, self-funded health insurance, and the valuation allowance for deferred tax assets.

2. INCOME TAXES

Income tax expense for the years ended December 31, 2014 and 2013 consists of the following:

	2014	2013
Current:		
Federal	$ 332,000	$ 91,000
State	15,000	1,000
	347,000	92,000
Deferred	(77,000)	153,000
	$ 270,000	$ 245,000

The expected provision for income taxes, computed by applying the U.S. federal income tax rate of 34% in 2014 and 34% in 2013 to income before taxes, is reconciled to income tax expense as follows:

	2014	2013
Expected provision for federal income taxes.	$ 312,000	$ 315,000
State income taxes, net of federal benefit	15,000	16,000
Domestic manufacturers deduction	(33,000)	(20,000)
Non-deductible meals, entertainment, and life insurance	21,000	13,000
Prior year adjustments............	(1,000)	(32,000)
Research and development credit	(31,000)	(45,000)
Valuation allowance released on capital loss utilized	(17,000)	-
Other............	4,000	(2,000)
	$ 270,000	$ 245,000

Net deferred tax liabilities consist of the following as of December 31, 2014 and 2013:

	2014	2013
Deferred tax assets:		
Accrued vacation	$ 23,000	$ 23,000
Inventories reserve............	129,000	105,000
Allowance for doubtful accounts	4,000	9,000
Allowance for sales returns............	13,000	13,000
Capital loss carryforward	-	309,000
Research and development credit carryforward	30,000	17,000
Accrued self-insured medical............	9,000	-
Less valuation allowance	(30,000)	(326,000)
	178,000	150,000
Deferred tax liabilities:		
Property and equipment	(462,000)	(468,000)
Intangible assets............	(83,000)	(59,000)
Net deferred tax liabilities	$ (367,000)	$ (377,000)

The deferred tax amounts described left have been included in the accompanying balance sheet as of December 31, 2014 and 2013 as follows:

	2014	2013
Current Assets	$ 178,000	$ 150,000
Noncurrent liabilities	(545,000)	(527,000)
	$ (367,000)	$ (377,000)

At December 31, 2013, the Company's valuation allowance of $326,000 related to a capital loss carryforward of $309,000 and a Minnesota research and development credit of $17,000. During the fourth quarter of 2014, the Company reversed $17,000 of the valuation allowance related to utilized capital loss carryforwards and wrote off the remaining $292,000 of capital loss carryforward that expired in the current year. The remaining valuation allowance balance of $30,000 at December 31, 2014 relates entirely to Minnesota research and development credit carryforwards that the Company does not expect to utilize and begin to expire in 2028.

It has been the Company's policy to recognize interest and penalties related to uncertain tax positions in income tax expense. As of December 31, 2014 and 2013, there was no liability for unrecognized tax benefits.

The Company is subject to federal and state taxation. The material jurisdictions that are subject to examination by tax authorities primarily include Minnesota and the United States, for tax years 2011, 2012, 2013 and 2014.

3. INTANGIBLE ASSETS

Intangible assets consist of patents, patent applications, licenses and covenants not to compete arising from business acquisitions. Capitalized patent application costs are included with patents. Intangible assets are amortized on a straight-line basis over their estimated useful lives or terms of their agreement, whichever is shorter. There were no impairment adjustments to intangible assets during the years ended December 31, 2014 or 2013.

Intangible assets at December 31, 2014 and 2013 consist of the following:

	December 31, 2014		December 31, 2013	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets:				
Patents............	$ 402,789	$ (62,676)	$ 345,790	$ (46,692)
Licenses............	50,000	(39,584)	50,000	(36,459)
Non-compete agreements	100,000	(96,658)	100,000	(89,992)
	$ 552,789	$ (198,918)	$ 495,790	$ (173,143)

Aggregate amortization expense:	2014	2013
For the years ended December 31	$25,775	$53,314

Estimated amortization expense for the years ending December 31:	
2015	23,000
2016	20,000
2017	20,000
2018	18,000
2019	16,000

In connection with the license agreement, the Company has agreed to pay royalties ranging from 3% to 5% on the sales of products subject to the agreements. The Company incurred $16,000 of expense under these agreements during 2014, and $19,000 during 2013 which have been included in selling, general and administrative expenses in the Statements of Income.

4. RETIREMENT PLAN

The Company has established a salary deferral plan under Section 401(k) of the Internal Revenue Code. Such deferrals accumulate on a tax-deferred basis until the employee withdraws the funds. The Company contributes up to 5% of each eligible employee's compensation. Total retirement expense for the years ended December 31, 2014 and 2013 was approximately $213,000 and $208,000, respectively.

5. SEGMENT INFORMATION

The Company's reportable segments are strategic business units that offer different products and have varied customer bases. There are five reportable segments: Domestic, Export, IKONICS Imaging, Digital Texturing (DTX) and AMS. Domestic sells screen printing film, emulsions, and inkjet receptive film to distributors located in the United States and Canada. IKONICS Imaging sells photo resistant film, art supplies, glass, metal medium and related abrasive etching equipment to end user customers located in the United States and Canada. AMS provides sound deadening 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. Export sells primarily the same products as Domestic and the IKONICS Imaging products not related to AMS or DTX. The accounting policies of the segments are the same as those described in the summary of significant accounting policies included in Note 1.

Management evaluates the performance of each segment based on the components of divisional income, and does not allocate assets and liabilities to segments except for trade receivables. Financial information with respect to the reportable segments follows:

For the year ended December 31, 2014:

	Domestic	Export	IKONICS Imaging	DTX	AMS	Unallocated*	Total
Net sales	$ 7,846,457	$ 5,249,843	$ 4,644,082	$ 422,646	$ 326,809	$ -	$ 18,489,837
Cost of goods sold	4,571,505	3,840,948	2,167,870	365,828	840,457	-	11,786,608
Gross profit (loss)	3,274,952	1,408,895	2,476,212	56,818	(513,648)	-	6,703,229
Selling, general and administrative*	1,353,509	549,254	918,337	166,724	425,087	1,711,853	5,124,764
Research and development*	-	-	-	-	-	664,999	664,999
Income (loss) from operations	$ 1,921,443	$ 859,641	$ 1,557,875	$ (109,906)	(938,735)	$ (2,376,852)	$ 913,466

For the year ended December 31, 2013:

	Domestic	Export	IKONICS Imaging	DTX	AMS	Unallocated*	Total
Net sales	$ 7,260,934	$ 5,641,544	$ 3,836,762	$ 407,193	$ 344,975	$ -	$ 17,491,408
Cost of goods sold	4,062,141	4,057,111	1,831,047	70,343	532,911	-	10,553,553
Gross profit	3,198,793	1,584,433	2,005,715	336,850	(187,936)	-	6,937,855
Selling, general and administrative*	1,307,154	578,084	977,574	474,782	446,803	1,584,003	5,368,400
Research and development*	-	-	-	-	-	649,325	649,325
Income (loss) from operations	$ 1,891,639	$ 1,006,349	$ 1,028,141	$ (137,932)	(634,739)	$ (2,233,328)	$ 920,130

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

Trade receivables by segment as of December 31, 2014 and December 31, 2013 were as follows:

	Dec 31, 2014	Dec 31, 2013
Domestic	$ 1,068,170	$ 1,012,057
Export	640,464	667,343
IKONICS Imaging	254,483	339,537
DTX	86,507	26,910
AMS	85,170	40,222
Unallocated	(38,466)	(35,216)
Total	$ 2,096,328	$ 2,050,853

6. STOCK OPTIONS

The Company has a stock incentive plan for the issuance of up to 442,750 shares of common stock. The plan provides for granting eligible participants stock options or other stock awards, as described by the plan, at option prices ranging from 85% to 110% of fair market value at date of grant. Options granted expire up to seven years after the date of grant. Such options generally become exercisable over a three year period. A total of 115,989 shares of common stock are reserved for additional grants of options under the plan at December 31, 2014.

Under the plan, the Company charged compensation cost of $18,415 and $13,907 against income in 2014 and 2013, respectively.

As of December 31, 2014, there was approximately $20,000 of unrecognized compensation cost related to unvested share-based compensation awards granted which is expected to be recognized over the next three years.

Proceeds from the exercise of stock options were $45,987 for 2014 and $89,398 for 2013.

The fair value of options granted during 2014 and 2013 were estimated using the Black-Scholes option pricing model with the following assumptions:

	2014	2013
Dividend yield	0%	0%
Expected volatility	44.3%	43.9%
Expected life of option	Five years	Five years
Risk-free interest rate	1.7%	0.7%
Fair values of each option on grant date	$11.49	$4.72

There were 1,250 options and 4,250 options granted during 2014 and 2013, respectively.

FASB ASC 718, Compensation – Stock Compensation specifies that initial accruals be based on the estimated number of instruments for which the requisite service is expected to be rendered. Therefore, the Company is required to incorporate a preexisting forfeiture rate based on the historical forfeiture experience and prospective actuarial analysis, estimated at 3%.

A summary of the status of the Company's stock option plan as of December 31, 2014 and changes during the year then ended is presented below:

Options	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value
Outstanding at January 1, 2014	11,417	$ 8.87		
Granted	1,250	28.25		
Exercised	(6,083)	7.56		
Expired and Forfeited	(1,666)	7.77		
Outstanding at December 31, 2014	4,918	$ 15.78	3.31	$ 33,126
Vested or expected to vest at December 31, 2014	4,918	$ 15.78	3.31	$ 33,126
Exercisable at December 31, 2014	916	$ 9.81	2.23	$ 9,846

The weighted-average grant date fair value of options granted was $11.49 and $4.72 for the years ended December 31, 2014 and 2013, respectively. The total intrinsic value of options exercised was $107,639 for the year ended December 31, 2014 and $95,477 for the year ended December 31, 2013.

There were 3,000 shares of restricted stock granted and subsequently forfeited, prior to vesting, during the year ended December 31, 2014. There were no restricted stock grants during the year ended December 31, 2013.

Restricted stock activity during the nine months ended December 31, 2014 was as follows:

	Shares	Weighted Average Price
Outstanding at January 1, 2014	-	$ -
Granted	3,000	28.25
Forfeited	3,000	28.25
Outstanding at December 31, 2014	-	$ -

7. CONCENTRATION OF CREDIT RISK

The Company maintains its cash balances primarily in two financial institutions. As of December 31, 2014, the balance at each of the institutions exceeded the Federal Deposit Insurance Corporation coverage.

Trade receivables are financial instruments that also expose the Company to concentration of credit risk. The large number of customers comprising the Company's customer base and their dispersion across different geographic areas limits such exposure. In addition, the Company routinely assesses the financial strength of its customers and maintains an allowance for doubtful accounts that management believes will adequately provide for credit losses.

8. LINE OF CREDIT

The Company has a $1,250,000 bank line of credit that provides for working capital financing. This line of credit is subject to renewal on May 31, 2015, is collateralized by trade receivables and inventories, and bears interest at 2.5 percentage points over 30-day LIBOR. There were no outstanding borrowings under this line of credit at December 31, 2014 and 2013. There are no financial covenants related to the line of credit.

COMMON STOCK

IKONICS Corporation common stock is traded on the Nasdaq Capital Market under the symbol IKNX. For investment and stock information contact:

JON GERLACH
Chief Financial Officer

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Phone: (218) 628-2217
email: jgerlach@ikonics.com

TRANSFER AGENT

WELLS FARGO SHAREOWNER SERVICES
PO Box 64854
St. Paul, MN 55164-0854

Shareholders with questions on stock holdings, transfer requirements and address changes contact Wells Fargo Bank at: (800) 468-9716

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COUNSEL

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Duluth, MN 55802
(218) 722-4766

ADDITIONAL FINANCIAL INFORMATION

For a copy of the Form 10-K, as filed with the Securities and Exchange Commission, and other financial information available at no charge to stockholders, please contact:

JON GERLACH
Chief Financial Officer

IKONICS Corporation
4832 Grand Avenue, Duluth, MN 55807
Phone: (218) 628-2217
email: jgerlach@ikonics.com

ANNUAL MEETING

The Company's annual meeting will be held:

April 30, 2015 1:00 p.m.

Kitchi Gammi Club
831 E. Superior Street
Duluth, MN 55802

Board of directors

LOCKWOOD CARLSON	President Carlson Consulting Group Minneapolis, MN **Director Since 2009**
RONDI C. ERICKSON	Chief Executive Officer (retired 2006) Apprise Technologies, Inc. Duluth, MN **Director Since 2000**
ERNEST M. HARPER, JR.	Chief Tax Officer (retired 2010) General Mills, Inc. Minneapolis, MN **Director Since 2012**
DAVID O. HARRIS	President David O. Harris, Inc. Minneapolis, MN **Director Since 1965**
DARRELL B. LEE	Vice President, Chief Financial Officer, Treasurer, Secretary MOCON, Inc. Minneapolis, MN **Director Since 2012**
H. LEIGH SEVERANCE	President Severance Capital Management Denver, CO **Director Since 2000**
GERALD W. SIMONSON	President Omnetics Connector Corporation Minneapolis, MN **Director Since 1978**
WILLIAM C. ULLAND	Chairman, President & CEO IKONICS Corporation Duluth, MN **Director Since 1972**

Corporate officers

WILLIAM C. ULLAND	**Chairman, President & CEO**
CLAUDE PIGUET	**Executive Vice President**
JON GERLACH	**Vice President, Finance, CFO**
ROBERT D. BANKS	**Vice President, International**
KEN HEGMAN	**Vice President, Sales: North America**

IKONICS®
Corporation

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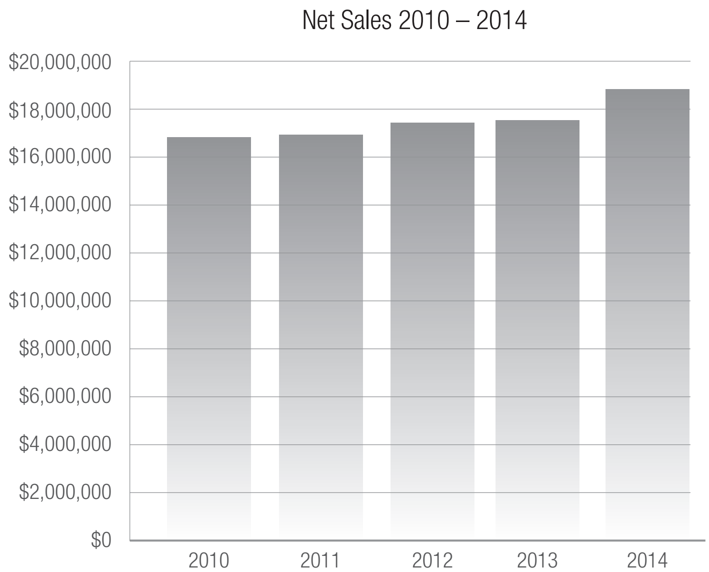

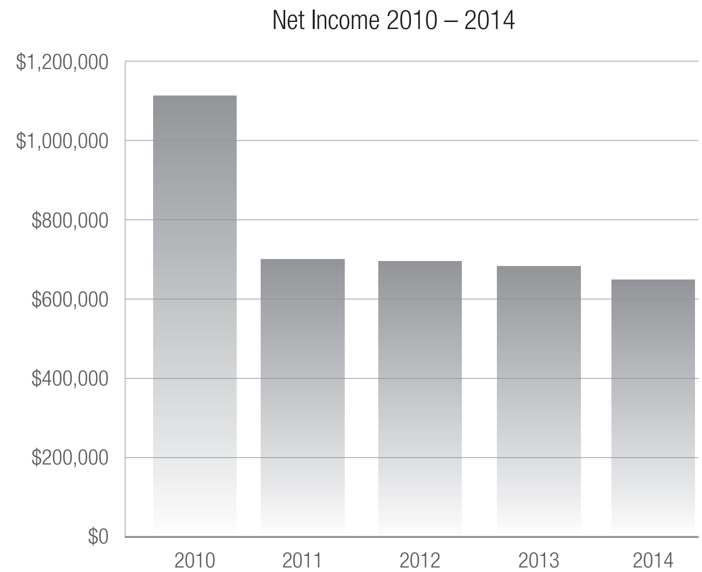

IKONICS Five-Year History	2010	2011	2012	2013	2014
Net Sales	$16,517,338	$16,780,262	$17,312,407	$17,491,408	$18,489,837
Pretax Income	$1,553,920	$1,043,257	$1,044,931	$927,173	$918,770
Net Income	$1,113,920	$698,257	$693,931	$682,173	$648,770
Net Cash Provided by Operations	$1,601,369	$793,532	$1,181,950	$1,466,532	$916,748
Return on Sales	6.7%	4.2%	4.0%	3.9%	3.5%
Return on Assets	8.5%	4.9%	5.3%	4.9%	4.4%
Return on Avg. Stockholders' Equity	9.6%	5.5%	5.6%	5.6%	5.0%
Debt to Equity	7.8%	9.1%	11.8%	11.1%	9.7%
Diluted EPS	$0.56	$0.35	$0.35	$0.34	$0.32
Stock price: High	$8.00	$8.94	$9.45	$19.45	$31.02
Low	$6.30	$6.90	$7.03	$7.92	$13.50
Close	$7.25	$7.57	$8.05	$14.75	$14.56
Weighted Average Common Shares Outstanding - Diluted	1,973,447	1,986,041	1,990,847	2,010,659	2,018,334
Total Assets	$13,141,931	$14,167,458	$13,184,276	$14,001,803	$14,627,962
Total Liabilities	$948,984	$1,176,915	$1,389,531	$1,401,985	$1,289,497
Total Stockholders' Equity	$12,192,947	$12,990,543	$11,794,745	$12,599,818	$13,338,465
Capital Spending	$189,150	$621,598	$566,519	$762,537	$434,463

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IKONICS® Corporation