
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549**

Form 10-Q

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2024

Or

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

Commission File Number 000-09587

ELECTRO-SENSORS, INC.

(Exact name of registrant as specified in its charter)

Minnesota

(State or other jurisdiction of incorporation or
organization)

41-0943459

(IRS Employer Identification No.)

6111 Blue Circle Drive

Minnetonka, Minnesota 55343-9108

(Address of principal executive offices)

(952) 930-0100

(Registrant's telephone number, including area code)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common stock, \$0.10 par value	ELSE	Nasdaq Capital Market

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Emerging growth company

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

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

The number of shares outstanding of the registrant's common stock, \$0.10 par value, on August 8, 2024 was 3,428,021.

ELECTRO-SENSORS, INC.
Form 10-Q
For the Period Ended June 30, 2024

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

ELECTRO-SENSORS, INC.
CONDENSED BALANCE SHEETS
(in thousands except share and per share amounts)

	June 30, 2024	December 31, 2023
	(unaudited)	
ASSETS		
Current assets		
Cash and cash equivalents	\$ 9,888	\$ 9,870
Investments	56	56
Trade receivables, less allowance for credit losses of \$11 and \$11, respectively	1,180	1,283
Inventories	1,865	1,751
Other current assets	177	179
Income tax receivable	41	0
Total current assets	13,207	13,139
Deferred income tax asset, net	330	355
Property and equipment, net	930	951
Total assets	\$ 14,467	\$ 14,445
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	\$ 199	\$ 291
Accrued expenses	439	323
Accrued income taxes	0	76
Total current liabilities	638	690
Commitments and contingencies		
Stockholders' equity		
Common stock par value \$0.10 per share; authorized 10,000,000 shares; 3,428,021 shares issued and outstanding	342	342
Additional paid-in capital	2,297	2,230
Retained earnings	11,190	11,183
Total stockholders' equity	13,829	13,755
Total liabilities and stockholders' equity	\$ 14,467	\$ 14,445

See accompanying notes to unaudited condensed financial statements

ELECTRO-SENSORS, INC.
CONDENSED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(in thousands except share and per share amounts)
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2024	2023	2024	2023
Net sales	\$ 2,217	\$ 2,137	4,461	4,182
Cost of goods sold	1,170	1,069	2,334	2,092
Gross profit	1,047	1,068	2,127	2,090
Operating expenses				
Selling and marketing	353	344	704	714
General and administrative	537	442	1,104	964
Research and development	264	238	526	506
Total operating expenses	1,154	1,024	2,334	2,184
Operating income (loss)	(107)	44	(207)	(94)
Non-operating income				
Interest expense	0	(1)	0	(1)
Interest income	109	95	225	188
Total non-operating income, net	109	94	225	187
Income before income tax expense	2	138	18	93
Income tax expense	6	22	11	21
Net income (loss)	\$ (4)	\$ 116	7	72
Other comprehensive income (loss)				
Change in unrealized value of available-for-sale securities, net of income tax	\$ 0	\$ 2	0	(2)
Other comprehensive income (loss)	0	2	0	(2)
Net comprehensive income (loss)	\$ (4)	\$ 118	7	70
Net income (loss) per share data:				
Basic				
Net income (loss) per share	\$ 0.00	\$ 0.03	0.00	0.02
Weighted average shares	3,428,021	3,428,021	3,428,021	3,428,021
Diluted				
Net income (loss) per share	\$ 0.00	\$ 0.03	0.00	0.02
Weighted average shares	3,428,021	3,443,394	3,428,021	3,443,930

See accompanying notes to unaudited condensed financial statements

ELECTRO-SENSORS, INC.
CONDENSED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(in thousands except share amounts)

For the three months ended June 30

	Common Stock Issued		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
	Shares	Amount				
March 31, 2024	3,428,021	\$ 342	\$ 2,259	\$11,194	\$ 0	\$ 13,795
Stock-based compensation expense			38			38
Net loss				(4)		(4)
Balance June 30, 2024 (unaudited)	<u>3,428,021</u>	<u>\$ 342</u>	<u>\$ 2,297</u>	<u>\$11,190</u>	<u>\$ 0</u>	<u>\$ 13,829</u>
March 31, 2023	3,428,021	\$ 342	\$ 2,163	\$10,864	\$ (3)	\$ 13,366
Other comprehensive income					2	2
Net income				116		116
Balance June 30, 2023 (unaudited)	<u>3,428,021</u>	<u>\$ 342</u>	<u>\$ 2,163</u>	<u>\$10,980</u>	<u>\$ (1)</u>	<u>\$ 13,484</u>

For the six months ended June 30

	Common Stock Issued		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
	Shares	Amount				
December 31, 2023	3,428,021	\$ 342	\$ 2,230	\$11,183	\$ 0	\$ 13,755
Stock-based compensation expense			67			67
Net income				7		7
Balance June 30, 2024 (unaudited)	<u>3,428,021</u>	<u>\$ 342</u>	<u>\$ 2,297</u>	<u>\$11,190</u>	<u>\$ 0</u>	<u>\$ 13,829</u>
December 31, 2022	3,428,021	\$ 342	\$ 2,163	\$10,908	\$ 1	\$ 13,414
Other comprehensive loss					(2)	(2)
Net income				72		72
Balance June 30, 2023 (unaudited)	<u>3,428,021</u>	<u>\$ 342</u>	<u>\$ 2,163</u>	<u>\$10,980</u>	<u>\$ (1)</u>	<u>\$ 13,484</u>

See accompanying notes to unaudited condensed financial statements

ELECTRO-SENSORS, INC.
CONDENSED STATEMENTS OF CASH FLOWS

(in thousands)
(unaudited)

	Six Months Ended June 30,	
	2024	2023
Cash flows from (used in) operating activities		
Net income	\$ 7	\$ 72
Adjustments to reconcile net income to net cash from (used in) operating activities:		
Depreciation	47	47
Deferred income taxes	25	(88)
Stock-based compensation expense	67	0
Change in:		
Trade receivables	103	(41)
Inventories	(114)	(170)
Other current assets	2	(10)
Accounts payable	(92)	82
Accrued expenses	116	81
Income tax payable/receivable	(117)	(20)
Net cash from (used in) operating activities	44	(47)
Cash flows used in investing activities		
Purchase of property and equipment	(26)	(1)
Net cash used in investing activities	(26)	(1)
Cash flows used in financing activities		
Payments on financing lease	0	(3)
Net cash used in financing activities	0	(3)
Net increase (decrease) in cash and cash equivalents	18	(51)
Cash and cash equivalents, beginning	9,870	9,626
Cash and cash equivalents, ending	\$ 9,888	\$ 9,575
Supplemental cash flow information		
Cash paid for income taxes	\$ 101	\$ 129
Cash paid for interest	0	1

See accompanying notes to unaudited condensed financial statements

ELECTRO-SENSORS, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
FOR THE PERIOD ENDED JUNE 30, 2024
(in thousands except share and per share amounts)
(unaudited)

Note 1. Basis of Presentation

The accompanying unaudited condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions and regulations of the Securities and Exchange Commission to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements.

This report should be read together with the Company's Annual Report on Form 10-K for the year ended December 31, 2023, including the audited financial statements and footnotes therein.

Management believes that the unaudited financial statements include all adjustments, consisting of normal recurring accruals, necessary to fairly state the financial position and results of operations as of June 30, 2024 and for the three and six-month periods ended June 30, 2024 and 2023, in accordance with accounting principles generally accepted in the United States of America. The results of interim periods may not be indicative of results to be expected for the year.

Nature of Business

Electro-Sensors, Inc. (the "Company") manufactures and markets a complete line of monitoring and control systems for a wide range of industrial machine applications. The Company uses leading-edge technology to continuously improve its products, with the goal of manufacturing the industry-preferred product for each of our served markets. The Company sells these products through an internal sales staff and distributors to a wide range of industries that use the products in a variety of applications to monitor process machinery operations. The Company markets its products to customers located throughout the United States, Canada, Latin America, Europe, and Asia.

Cash and 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 are invested in commercial paper, money market accounts and may, also, be invested in Treasury Bills with an original maturity of three months or less. Cash equivalents are carried at fair value.

The Company maintains its cash and cash equivalents primarily in two bank deposit accounts, which, at times, may exceed federally insured limits. The Company has not experienced any losses on these accounts. The Company believes it is not exposed to significant credit risk on cash.

Trade receivables and credit policies

Trade receivables are uncollateralized customer obligations due under normal trade terms generally requiring payment within 30 days from the invoice date. Trade receivables are stated at the amount billed to the customer. Customer account balances with invoices over 90 days are considered delinquent. The Company does not accrue interest on delinquent trade receivables.

Payments of trade receivables are allocated to the specific invoices identified on the customer's remittance advice or, if unspecified, are applied to the earliest unpaid invoices.

ELECTRO-SENSORS, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
FOR THE PERIOD ENDED JUNE 30, 2024
(in thousands except share and per share amounts)
(unaudited)

The Company maintains an allowance for credit losses on trade receivables, which is recorded as an offset to trade receivables. Changes in the allowance for credit losses are included as a component of operating expenses in the Statements of Comprehensive Income (Loss). The Company assesses credit losses on its entire balance of trade receivables.

The allowance is based on the credit losses expected to arise over the life of the receivable (contractual term). The Company considers historical loss rates and current economic conditions when determining the expected credit losses. Receivables are written off against the allowance for credit losses. The allowance for credit losses was \$11 at June 30, 2024 and December 31, 2023.

Revenue Recognition

At contract inception, the Company assesses the goods and services to be provided to a customer and identifies a performance obligation for each distinct good or service. We also determine the transaction price for each performance obligation at contract inception. Our contracts, generally in the form of a purchase order, specify the product or service that is to be provided to the customer. The typical contract life is less than one month and contains a single performance obligation, which is to provide conforming goods or services to the customer. Certain contracts have a second performance obligation, which typically is the initialization of the HazardPRO™ product. For contracts that have multiple performance obligations, we allocate the transaction price to each performance obligation using the relative stand-alone selling price. We generally determine stand-alone selling prices based on the observable stand-alone prices charged to customers. We recognize product revenue at the point in time when control of the product is transferred to the customer, which typically occurs when we ship the products. We recognize service revenue at the point in time when we have provided the service, which typically takes less than a week to provide.

Fair Value Measurements

The carrying value of cash equivalents, trade receivables, accounts payable, and other financial working capital items approximates fair value at June 30, 2024 and December 31, 2023, due to the short maturity nature of these instruments.

Stock-Based Compensation

The Company records compensation expense for stock options based on the estimated fair value of the options on the date of grant using the Black-Scholes-Merton (“BSM”) option pricing model. The Company uses historical data, among other factors, to estimate the expected price volatility, the expected option life, and the expected forfeiture rate. The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for the estimated life of the option.

ELECTRO-SENSORS, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
FOR THE PERIOD ENDED JUNE 30, 2024
(in thousands except share and per share amounts)
(unaudited)

Use of Estimates

The preparation of 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 amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Current significant estimates, including the underlying assumptions, consist of economic lives of long-lived assets, realizability of trade receivables, and valuation of deferred tax assets/liabilities, inventory, investments, and stock compensation expense. It is at least reasonably possible that these estimates may change in the near term.

Net Income (Loss) per Common Share

Basic income (loss) per share excludes dilution and is determined by dividing net income (loss) by the weighted-average number of common shares outstanding during the period. Diluted net income (loss) per share reflects the potential dilution that could occur if securities such as options or restricted stock units were exercised or converted into common stock.

Diluted earnings per share ("Diluted EPS") considers the impact of potentially dilutive securities except in periods in which there is a loss because the inclusion of the potential shares would have an anti-dilutive effect. Diluted EPS also excludes the impact of common shares issuable upon the exercise of outstanding stock options in periods in which the option exercise price is greater than the average market price of our common stock during the period.

For the three-month periods ended June 30, 2024, and 2023, 175,000 and 284,627 respectively, weighted-average common shares for underlying stock options have been excluded from the calculation of diluted EPS because their effect would be anti-dilutive. For the six-month periods ended June 30, 2024 and 2023, 175,000 and 284,091 respectively, weighted average common shares for underlying stock options have been excluded from the calculation.

In addition, for each of the three and six-month periods ended June 30, 2024, 105,000 restricted stock units have been excluded from the calculation of diluted EPS because their effect would be anti-dilutive.

Reclassification of Prior Year Presentation

All Treasury Bills have been reclassified to cash equivalents for consistency with the current year presentation. The reclassification had no effect on the reported results of operations. The Balance Sheet and Statement of Cash Flows have been adjusted to reflect this reclassification.

ELECTRO-SENSORS, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
FOR THE PERIOD ENDED JUNE 30, 2024
(in thousands except share and per share amounts)
(unaudited)

Note 2. Investments

The Company has investments in common equity securities of two private U.S. companies.

Equity securities are stated at estimated fair value and realized and unrealized gains and losses, if any, are reported in our Statements of Comprehensive Income (Loss) in non-operating income.

The cost and estimated fair value of the Company's investments are as follows:

	Cost	Gross unrealized gain	Gross unrealized loss	Fair value
June 30, 2024				
Equity Securities	\$ 54	\$ 2	\$ 0	\$ 56
Total Investments, June 30, 2024	<u>\$ 54</u>	<u>\$ 2</u>	<u>\$ 0</u>	<u>\$ 56</u>
December 31, 2023				
Equity Securities	\$ 54	\$ 2	\$ 0	\$ 56
Total Investments, December 31, 2023	<u>\$ 54</u>	<u>\$ 2</u>	<u>\$ 0</u>	<u>\$ 56</u>

ELECTRO-SENSORS, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
FOR THE PERIOD ENDED JUNE 30, 2024
(in thousands except share and per share amounts)
(unaudited)

Note 3. Fair Value Measurements

The following table provides information on those assets and liabilities measured at fair value on a recurring basis.

June 30, 2024

	Carrying amount in balance sheet	Fair Value	Fair Value Measurement Using		
			Level 1	Level 2	Level 3
Assets:					
Equity Securities	\$ 56	\$ 56	\$ 0	\$ 0	\$ 56

December 31, 2023

	Carrying amount in balance sheet	Fair Value	Fair Value Measurement Using		
			Level 1	Level 2	Level 3
Assets:					
Equity Securities	\$ 56	\$ 56	\$ 0	\$ 0	\$ 56

The equity securities owned by the Company are investments in two non-publicly traded companies. There is an undeterminable market for each of these two companies and the Company has determined the fair value based on financial and other factors that are considered level 3 inputs in the fair value hierarchy.

The changes in level 3 assets measured at fair value on a recurring basis are as follows:

	Six Months Ended June 30,	
	2024	2023
Beginning Balance	\$ 56	\$ 56
Change in Fair Value	0	0
Ending Balance	<u>\$ 56</u>	<u>\$ 56</u>

Note 4. Inventories

Inventories used in the determination of cost of goods sold are as follows:

	June 30, 2024	December 31, 2023
Raw Materials	\$ 1,192	\$ 1,172
Work In Process	336	301
Finished Goods	347	288
Reserve for Obsolescence	(10)	(10)
Total Inventories, net	<u>\$ 1,865</u>	<u>\$ 1,751</u>

ELECTRO-SENSORS, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
FOR THE PERIOD ENDED JUNE 30, 2024
(in thousands except share and per share amounts)
(unaudited)

Note 5. Stock-Based Compensation

Stock options

The 2013 Equity Incentive Plan (the “2013 Plan”) authorizes the issuance of nonqualified stock options. Payment for the shares may be made in cash, shares of the Company’s common stock or a combination thereof. Under the terms of the 2013 Plan, non-qualified stock options are granted at a minimum of 100% of fair market value on the date of grant and may be exercised at various times depending upon the terms of the option. All existing options expire 10 years from the date of grant, subject to early termination 12 months after termination of employment or service due to death, disability, or termination other than for cause. The grants include a provision providing for acceleration of vesting upon a change of control in the Company.

As of June 30, 2024, the total unrecognized compensation expense related to outstanding stock options was \$124, which the Company expects to recognize through April 2028. The Company recognized compensation expense in connection with the vesting of stock options of approximately \$16 and \$24 for the three and six months ended June 30, 2024, respectively. There was no stock compensation expense related to stock option grants recognized in the six months ended June 30, 2023.

During the second quarter of 2024, the Company granted 25,000 non-qualified stock options to one of its non-employee board members. The options vest 20% on the grant date, with an additional 20% vesting annually thereafter. There were no stock options exercised in the six months ended June 30, 2024. There were no stock options granted or exercised in the six months ended June 30, 2023.

The assumptions made in estimating the fair value of the options on the grant date based upon the BSM option-pricing model during the three-month period ended June 30, 2024 are as follows:

Dividend Yield	0.00%
Expected Volatility	25.07%
Risk Free Interest Rate	4.65%
Expected Life	6 Years

The Company calculates expected volatility for stock options and other awards using historical volatility as the Company believes the expected volatility will approximate historical volatility.

ELECTRO-SENSORS, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
FOR THE PERIOD ENDED JUNE 30, 2024
(in thousands except share and per share amounts)
(unaudited)

The following table summarizes the activity for all stock options outstanding for the six months ended June 30:

	2024		2023	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Options outstanding at beginning of year	175,000	\$ 4.06	300,000	\$ 4.35
Granted	25,000	4.13	0	
Exercised	0		0	
Expired	(25,000)	4.39	0	
Options outstanding at June 30	175,000	\$ 4.04	300,000	\$ 4.35
Options exercisable at June 30	75,000	\$ 3.68	300,000	\$ 4.35

Restricted stock units

The 2013 Plan authorizes the issuance of restricted stock units. Stock-based compensation expense is determined on the grant date based on the closing market value of the Company's common stock. The amount of expense is calculated based on an estimate of the number of awards expected to vest at the end of each vesting period and is expensed evenly over the vesting period. In connection with the time of vesting and issuance of shares, an eligible recipient of common stock may elect to have some shares withheld by the Company to satisfy any requirement for withholding taxes. The grants include a provision providing for acceleration of vesting upon a change of control in the Company.

As of June 30, 2024, the total unrecognized compensation expenses related to outstanding restricted stock units is \$360, which the Company expects to recognize through August 2028. The Company recognized compensation expense in connection with the vesting of restricted stock units of approximately \$22 and \$43 for the three and six months ended June 30, 2024, respectively. There was no stock compensation expense related to restricted stock unit grants recognized in the six months ended June 30, 2023.

There were no restricted stock units granted or exercised in the six months ended June 30, 2024 and 2023.

Note 6. Contingencies

The Company at times becomes subject to claims against it in the ordinary course of business. There are currently no pending or threatened claims against the Company that it believes will have a material adverse effect on its results of operations or liquidity.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

FORWARD-LOOKING STATEMENTS

The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements made by us or on our behalf. We have made, and may continue to make, forward-looking statements with respect to our business and financial matters, including statements contained in this document, other filings with the Securities and Exchange Commission, and reports to shareholders. Forward-looking statements generally include discussion of current expectations or forecasts of future events and can be identified by the use of terminology such as “believe,” “estimate,” “expect,” “intend,” “may,” “could,” “will,” and similar words or expressions. Any statement that does not relate solely to historical fact should be considered forward-looking.

Our forward-looking statements generally relate to our growth strategy, future financial results, product development, and sales efforts. We make forward-looking statements throughout this Form 10-Q, but primarily in this Management’s Discussion and Analysis of Financial Condition and Results of Operations section. These include statements relating to our beliefs and expectations and intentions with respect to (i) our growth and profitability, (ii) our marketing and product development, (iii) our ability to continue to obtain parts and materials for our products from various manufacturers and distributors in a timely manner and at reasonable prices, (iv) the value of our intellectual property, (v) our competitive position in the marketplace, (vi) the effect of governmental regulations on our business, (vii) our employee relations, (viii) the adequacy of our facilities, (ix) our intention to develop new products, (x) the possibility of us acquiring compatible businesses or product lines as part of our growth strategy, and (xi) our future cash requirements and use of cash.

Forward-looking statements cannot be guaranteed and our actual results may vary materially due to the uncertainties and risks, known and unknown, associated with these statements, including our ability to successfully develop new products and manage our cash requirements. We undertake no obligation to update any forward-looking statements. We cannot foresee or identify all factors that could cause actual results to differ from expected or historical results. As such, investors should not consider any list of these factors to be an exhaustive statement of all risks, uncertainties, or potentially inaccurate assumptions. These forward-looking statements are subject to certain risks and uncertainties that could cause future results to differ materially from our recent results listed under the heading “Forward-Looking Statements” under “Item 1—Business,” in our Annual Report on Form 10-K for the year ended December 31, 2023.

CRITICAL ACCOUNTING ESTIMATES

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make decisions based upon estimates, assumptions, and factors it considers relevant to the circumstances. These decisions include the selection of applicable accounting principles and the use of judgment in their application and affect reported amounts and disclosures. Changes in economic conditions or other business circumstances may affect the outcomes of management’s estimates and assumptions. An in-depth description of our accounting estimates can be found in the interim financial statements included in this report and in our Annual Report on Form 10-K for the fiscal year ended December 31, 2023. There have been no changes to our critical accounting estimates during the three and six-month periods ended June 30, 2024.

SELECTED FINANCIAL INFORMATION

The following table contains selected financial information, for the periods indicated, from our Condensed Statements of Comprehensive Income (Loss) expressed as a percentage of net sales.

	Three Months Ended June 30		Six Months Ended June 30	
	2024	2023	2024	2023
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of goods sold	52.8	50.0	52.3	50.0
Gross profit	47.2	50.0	47.7	50.0
Operating expenses				
Selling and marketing	15.9	16.1	15.8	17.0
General and administrative	24.2	20.7	24.7	23.1
Research and development	11.9	11.1	11.8	12.1
Total operating expenses	52.0	47.9	52.3	52.2
Operating income (loss)	(4.8)	2.1	(4.6)	(2.2)
Non-operating income				
Interest income	4.9	4.4	5.0	4.5
Total non-operating income, net	4.9	4.4	5.0	4.5
Income before income tax expense	0.1	6.5	0.5	2.3
Income tax expense	0.3	1.0	0.2	0.5
Net income (loss)	(0.2)%	5.5%	0.3%	1.8%

The following paragraphs discuss the Company's performance for the three and six months ended June 30, 2024 and 2023.

RESULTS OF OPERATIONS (in thousands)

Net Sales

Net sales for the second quarter of 2024 were \$2,217, an increase of \$80, or 3.7%, from \$2,137 during the comparable period in 2023. Net sales for the six months ended June 30, 2024 were \$4,461, an increase of \$279, or 6.7%, from \$4,182 during the comparable period in 2023. The increase during the three-month period was due to higher sales of HazardPRO wireless hazard monitoring systems for agricultural applications.

Gross Profit

Gross profit for the second quarter of 2024 was \$1,047, a decrease of \$21, or 2.0%, over the same period in 2023. Gross profit for the six months ended June 30, 2024 was \$2,127, an increase of \$37, or 1.8%, over the same period in 2023. Gross margin decreased in the second quarter of 2024 to 47.2% from 50.0% during the same period in 2023. Gross margin for the six months ended June 30, 2024 decreased to 47.7% from 50.0% over the same period in 2023. The decrease in gross margin was primarily due to an increase in material and labor costs across all product lines.

Operating Expenses

Total operating expenses increased \$130, or 12.7%, to \$1,154 for the second quarter of 2024 compared to the same period in 2023 and increased as a percentage of net sales to 52.0% from 47.9%. Total operating expenses increased \$150, or 6.9%, to \$2,334 for the six months ended June 30, 2024 compared to the same period in 2023 and increased as a percentage of net sales to 52.3% from 52.2%. The increase in operating expenses for both periods was primarily due to additional headcount and stock-based compensation related to the granting of stock options and restricted stock units in the current quarter and third quarter of 2023.

- Selling and marketing expenses in the second quarter of 2024 increased \$9 to \$353, or 2.6%, from the same period in 2023 and decreased as a percentage of net sales to 15.9% from 16.1%. Selling and marketing expenses in the six months ended June 30, 2024 decreased \$10 to \$704, or 1.4%, from the same period in 2023 and decreased as a percentage of net sales to 15.8% from 17.0%. The increase for the three-month period was primarily due to increased employee benefits expenses and higher trade show expenses. The decrease for the six-month period was primarily due to decreased customer focused marketing expenses and change in sales staff.
- General and administrative expenses increased \$95 to \$537, or 21.5%, in the second quarter of 2024 compared to the same period in 2023 and increased as a percentage of net sales to 24.2% from 20.7%. General and administrative expenses increased \$140 to \$1,104, or 14.5%, in the six months ended June 30, 2024 compared to the same period in 2023 and increased as a percentage of net sales to 24.7% from 23.1%. The increase in the second quarter was primarily due to an increase in stock-based compensation and contract labor costs. The increase in the six-month period was primarily due to an increase in stock-based compensation and contract labor costs, partially offset by a decrease in legal and professional fees.
- Research and development expenses increased \$26 to \$264, or 10.9%, in the second quarter of 2024 compared to the same period in 2023 and increased as a percentage of net sales to 11.9% from 11.1%. Research and development expenses increased \$20 to \$526, or 4.0%, in the six months ended June 30, 2024 compared to the same period in 2023 but decreased as a percentage of net sales to 11.8% from 12.1%. The increase for the three-month period was due to additional headcount. The increase for the six-month period was due to additional headcount, partially offset by lower contract engineering costs related to product development and enhancements.

Non-Operating Income

Net non-operating income increased by \$15, or 16.0%, for the three-month period ended June 30, 2024 compared to the same period in 2023. Net non-operating income increased by \$38, or 20.3%, for the six months ended June 30, 2024 compared to the same period in 2023. The increase for both periods is the result of additional interest income earned as a result of higher interest rates on Treasury Bills.

Income Before Income Tax Expense

Income before income tax expense was \$2 for the three-month period ended June 30, 2024, representing a decrease of \$136 compared to \$138 for the same period in 2023. Income before income tax expense was \$18 for the six months ended June 30, 2024, representing a decrease of \$75 compared to \$93 for the same period in 2023. The decrease in both periods was primarily due to lower gross margins and higher operating expenses, partially offset by an increase in interest income, as discussed above.

Income Tax Expense

Income tax expense was \$6, or 0.3%, of net sales in the second quarter of 2024 compared to \$22, or 1.0%, of net sales in the second quarter of 2023. Income tax expense was \$11, or 0.2% of net sales for the six months ended June 30, 2024 compared to \$21, or 0.5% of net sales for the six months ended June 30, 2023. The effective tax rate for the six-month period ended June 30, 2024 was 61.1% compared to 22.6% in the same period of 2023. The change in the effective tax rate is due to non-deductible stock-based compensation expense.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents were \$9,888 at June 30, 2024 and \$9,870 at December 31, 2023. The increase was primarily the result of an increase in cash from operating activities.

Cash from operating activities was \$44 for the six months ended June 30, 2024 as compared to cash used in operating activities of \$47 for the six months ended June 30, 2023. The \$91 increase in cash from operating activities was due primarily to a change in deferred taxes, an increase in stock-based compensation expense, and a decrease in trade receivables, partially offset by a decrease in accounts payable. The decrease in trade receivables is due to the timing of sales and collections. The decrease in accounts payable is due to the timing of inventory receipts and payment of invoices.

Cash used in investing activities was \$26 and \$1 for the six months ended June 30, 2024 and 2023, respectively. The cash used was for the purchase of office equipment.

Cash used in financing activities in the six months ended June 30, 2023 was \$3. There was no cash flow from financing activities in the six months ended June 30, 2024.

Subject to the following section, entitled "Supply Chain and Labor Dynamics," the Company believes its ongoing cash requirements will be primarily for capital expenditures, research, and development, working capital, corporate and business development, and other strategic alternatives and that existing cash, cash equivalents, and investments and any cash generated from operations will be sufficient to meet these cash requirements through at least the next 12 months.

Supply Chain and Labor Dynamics

We strive to have multiple sources of production components and materials. However, we continue to experience disruptions in our supply chain, resulting in difficulty sourcing certain components. We are also experiencing price increases for many of the components used in our products. To meet these challenges, we are seeking additional sources for components and modifying product designs to accommodate new components that are more readily available at competitive prices. There is no guarantee that we will continue to be successful in modifying these designs and sourcing alternative components. As a result, we could experience significant delays in receiving certain components needed to make timely customer deliveries, as well as increased costs that erode gross margins. Supply chain dynamics may have an effect on the efficiency of our business operations, our customer base, and the domestic or worldwide economy. Furthermore, the labor market for qualified employees able to fill our various open positions is challenging and may result in delays in filling these positions and increased labor costs. In addition, we may experience changes in transportation and freight availability that may make it difficult to have materials and components shipped to us, or our products shipped to customers, in a timely and cost-effective manner. While we continue to closely manage each of these activities, our actions may not be successful and may result in a negative effect on our sales and profit margins.

Future Corporate and Business Development Activities

We continue to seek growth opportunities, both internally through our existing portfolio of products, technologies, and markets, as well as externally through technology partnerships or related-product or business acquisitions. In addition, we continue to explore other strategic alternatives that we believe present good opportunities for the Company and its shareholders. The Company's Board of Directors has a special committee to explore and pursue business development and other strategic alternatives.

Off-balance Sheet Arrangements

As of June 30, 2024, the Company had no off-balance sheet arrangements or transactions.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Not Applicable.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Based on an evaluation with the participation of the Company's management, the Company's principal executive officer and principal financial officer has concluded that the Company's disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("Exchange Act"), were effective as of June 30, 2024.

Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting during the second quarter of 2024 that were identified in connection with management's evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Exchange Act, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings – None

Item 1A. Risk Factors – Not Applicable

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds – None

Item 3. Defaults Upon Senior Securities – None

Item 4. Mine Safety Disclosures – Not Applicable

Item 5. Other Information – None

Item 6. Exhibits

<u>Exhibit</u>	<u>Description</u>
31.1	Certification of CEO and CFO Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of CEO and CFO Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	The following financial information from Electro-Sensors, Inc.'s Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2024, formatted in iXBRL (Inline Extensible Business Reporting Language), (i) Condensed Balance Sheets as of June 30, 2024 and December 31, 2023, (ii) Condensed Statements of Comprehensive Income (Loss) for the three and six months ended June 30, 2024 and June 30, 2023, (iii) Condensed Statements of Changes in Stockholders' Equity for the three and six months ended June 30, 2024 and June 30, 2023, (iv) Condensed Statements of Cash Flows for the six months ended June 30, 2024 and June 30, 2023, and (v) Notes to Financial Statements.

SIGNATURES

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

Electro-Sensors, Inc.

August 9, 2024

/s/ David L. Klenk

David L. Klenk
Chief Executive Officer and Chief Financial Officer
(Principal Executive Officer and Principal Financial
Officer)

**CERTIFICATION PURSUANT TO
SECTION 302 OF THE SARBANES OXLEY-ACT OF 2002**

I, David L. Klenk, certify that:

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

August 9, 2024

/s/ David L. Klenk

David L. Klenk
Chief Executive Officer and Chief Financial Officer

**CERTIFICATION PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Electro-Sensors, Inc. (the “Company”) on Form 10-Q for the quarter ended June 30, 2024 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, David L. Klenk, Chief Executive Officer and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

August 9, 2024

/s/ David L. Klenk
David L. Klenk
Chief Executive Officer and Chief Financial Officer