INTERLINK ELECTRONICS INC
Form 10-Q
August 10, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 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, 2017

or

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

For the transition period from __________________ to ______________________.

Commission file number 001-37659

INTERLINK ELECTRONICS, INC.

(Exact name of registrant as specified in its charter)

Nevada	77-0056625
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

31248 Oak Crest Drive, Suite 110
Westlake Village, California 91361

(Address of principal executive offices, zip code)

(805) 484-8855

(Registrant's telephone number, including area code)

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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post 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	(Do not check if smaller reporting company)	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

As of August 10, 2017, the issuer had 7,336,488 shares of common stock issued and outstanding.

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INTERLINK ELECTRONICS, INC.

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PART I: FINANCIAL INFORMATION

Item 1.Financial Statements

INTERLINK ELECTRONICS, INC.

Condensed Consolidated Balance Sheets

(unaudited)

	June 30, 2017	December 31, 2016
	(in thousands, except par value)	
ASSETS		
Current assets		
Cash and cash equivalents	$ 6,968	$ 6,009
Restricted cash	5	5
Accounts receivable, net	1,958	1,726
Inventories	1,361	1,268
Prepaid expenses and other current assets	214	377
Total current assets	10,506	9,385
Property, plant and equipment, net	272	310
Intangibles, net	56	44
Deferred income taxes	622	675
Other assets	58	57
Total assets	$ 11,514	$ 10,471
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$ 335	$ 324
Accrued liabilities	303	334
Accrued income taxes	201	104
Deferred revenue, current	44	111
Total current liabilities	883	873
Total liabilities	883	873
Commitments and contingencies (see note 9)		
Stockholders' equity		
Preferred stock, $0.01 par value: 1,000 shares authorized, no shares issued or outstanding	—	—
Common stock, $0.001 par value: 30,000 shares authorized, 7,335 and 7,326 shares issued and outstanding at June 30, 2017 and December 31, 2016,	7	7

respectively		
Additional paid-in-capital	60,454	60,370
Accumulated other comprehensive (loss) income	(35)	(71)
Accumulated deficit	(49,795)	(50,708)
Total stockholders' equity	10,631	9,598
Total liabilities and stockholders' equity	$ 11,514	$ 10,471

The accompanying notes are an integral part of these condensed consolidated financial statements.

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INTERLINK ELECTRONICS, INC.

Condensed Consolidated Statements of Income

(unaudited)

	Three months ended June 30, 2017	2016	Six months ended June 30, 2017	2016
	(in thousands, except per share data)			
Revenue, net	$ 3,264	$ 3,054	$ 6,148	$ 5,859
Cost of revenue	1,203	1,211	2,351	2,345
Gross profit	2,061	1,843	3,797	3,514
Operating expenses:				
Engineering, research and development	157	174	335	315
Selling, general and administrative	1,065	755	2,092	1,667
Total operating expenses	1,222	929	2,427	1,982
Income from operations	839	914	1,370	1,532
Other income (expense):				
Other income (expense), net	(2)	15	17	29
Income before income tax expense	837	929	1,387	1,561
Income tax expense	288	180	474	206
Net income	549	749	913	1,355
Other comprehensive income, net of tax:				
Foreign currency translation adjustments	25	(25)	36	(21)
Comprehensive income	$ 574	$ 724	$ 949	$ 1,334
Earnings per share, basic and diluted	$ 0.07	$ 0.10	$ 0.12	$ 0.18
Weighted average common shares outstanding - basic	7,333	7,326	7,331	7,326
Weighted average common shares outstanding - diluted	7,420	7,406	7,416	7,400

The accompanying notes are an integral part of these condensed consolidated financial statements.

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INTERLINK ELECTRONICS, INC.

Condensed Consolidated Statements of Cash Flows

(unaudited)

	Six months ended June 30,	
	2017	2016
	(in thousands)	
Cash flows from operating activities:		
Net income	$ 913	$ 1,355
Adjustments to reconcile net income from continuing operations to net cash provided by operating activities:		
Depreciation and amortization	86	34
Stock based compensation	50	43
Changes in operating assets and liabilities:		
Accounts receivable	(232)	(136)
Inventories	(93)	(270)
Prepaid expenses and other current assets	163	90
Other assets	(1)	(35)
Accounts payable	11	120
Accrued liabilities	(31)	(18)
Accrued income taxes	97	—
Deferred income taxes	53	—
Deferred revenue	(67)	(27)
Net cash provided by operating activities	949	1,156
Cash flows from investing activities:		
Property, plant and equipment	(41)	(166)
Intangibles	(19)	—
Net cash used in investing activities	(60)	(166)
Cash flows from financing activities:		
Proceeds from exercise of stock options	34	—
Net cash provided by financing activities	34	—
Effect of exchange rate changes on cash and cash equivalents	36	(21)
Net increase in cash and cash equivalents	959	969
Cash and cash equivalents, beginning of period	6,009	4,430
Cash and cash equivalents, end of period	$ 6,968	$ 5,399
Supplemental disclosure of cash flow information:		
Income taxes paid	$ 293	$ 22

The accompanying notes are an integral part of these condensed consolidated financial statements.

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INTERLINK ELECTRONICS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

NOTE 1-THE COMPANY AND ITS SIGNIFICANT ACCOUNTING POLICIES

Description of Business

Interlink Electronics, Inc. ("we," "us," "our," "Interlink" or the "Company") designs, develops, manufactures and sells a range force-sensing technologies that incorporate our proprietary materials technology, firmware and software into a portfolio of standard sensor based products and custom sensor system solutions. These include sensor components, subassemblies, modules and products that support effective, efficient cursor control and novel three-dimensional user inputs. Our human machine interface ("HMI") technology platforms are deployed in a wide range of markets including consumer electronics, automotive, industrial, and medical.

Interlink serves our world-wide customer base from our corporate headquarters in Westlake Village, California (greater Los Angeles area), our global research and development ("R&D") and engineering center in Singapore, our printed-electronics manufacturing facility in Shenzhen, China and our global distribution and logistics center in Hong Kong. We also maintain engineering, assembly and prototyping capabilities in Simi Valley, California along with technical and sales offices in Japan and at multiple locations in the United States. Our principal executive office is located at 31248 Oak Crest Drive, Suite 110, Westlake Village, California 91361 and our telephone number is (805) 484-8855. Our website address is www.interlinkelectronics.com.

Fiscal Year

Our fiscal year is January 1 through December 31.

Basis of Presentation

The interim unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial information. They do not include all of the information and footnotes required by GAAP for complete financial statements. The December 31, 2016 balance sheet data was derived from the Company’s audited consolidated financial statements, but does not include all disclosures required for annual periods. Therefore, these unaudited condensed consolidated financial statements should be read in conjunction with our audited consolidated financial statements and notes thereto for the year ended December 31, 2016, included in our Annual Report on Form 10-K, filed with the SEC on March 2, 2017.

The condensed consolidated financial statements included herein are unaudited. However, they contain all normal recurring accruals and adjustments that, in the opinion of management, are necessary to present fairly our consolidated financial position and our consolidated results of operations and consolidated cash flows. The results of operations for the three and six months ended June 30, 2017 are not necessarily indicative of the results to be expected for future quarters or the full year.

Our condensed consolidated financial statements include the accounts of Interlink and our subsidiaries in Shenzhen, China, Hong Kong and Singapore. All intercompany accounts and transactions between our consolidated operations have been eliminated.

Share and per share amounts and weighted-average grant date fair value reflect a 25% stock dividend paid on April 1, 2016.

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INTERLINK ELECTRONICS, INC.

Notes to Condensed Consolidated Financial Statements - continued

(unaudited)

Foreign Currency Translation

The functional currency of our Chinese subsidiary is the Chinese Yuan Renminbi. The functional currency for our Hong Kong and Singapore subsidiaries is the United States dollar. However, our Hong Kong and Singapore subsidiaries also transact business in their local currency. Therefore, assets and liabilities are translated into United States dollars at the exchange rate in effect on the balance sheet date. Revenues and expenses are translated at the average exchange rate prevailing during the respective periods. Foreign currency transaction and translation gains and losses are included in results of operations.

Segment Reporting

We operate in one reportable segment: the manufacture and sale of force sensing technology solutions.

Use of Estimates

The preparation of consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and disclosures made in the accompanying notes to the consolidated financial statements. Management regularly evaluates estimates and assumptions related to revenue recognition, allowances for doubtful accounts, warranty reserves, inventory valuation reserves, stock-based compensation, purchased intangible asset valuations and useful lives, asset retirement obligations, and deferred income tax asset valuation allowances. These estimates and assumptions are based on current facts, historical experience and various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about carrying values of assets and liabilities that are not readily apparent from other sources. The actual results we experience may differ materially and adversely from our original estimates. To the extent there are material differences between the estimates and the actual results, our future results of operations will be affected.

Risk and Uncertainties

Our future results of operations involve a number of risks and uncertainties. Factors that could affect our business or future results and cause actual results to vary materially from historical results include, but are not limited to, the rapid change in our industry; problems with the performance, reliability or quality of our products; loss of customers; impacts of doing business internationally, including foreign currency fluctuations; potential shortages of the supplies we use to manufacture our products; disruptions in our manufacturing facilities; changes in environmental directives impacting our manufacturing process or product lines; the development of new proprietary technology and the enforcement of intellectual property rights by or against us; our ability to attract and retain qualified employees; and our ability to raise additional capital.

Recently Adopted Accounting Pronouncements

In June 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2014-12, “Compensation—Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period (a consensus of the FASB Emerging Issues Task Force)”, effective for annual periods and interim periods within those annual periods, beginning after December 15, 2015. This update is intended to resolve the diverse accounting treatment of share-based payment awards whose performance target may be achieved after the requisite service period. An entity may apply the standards (1) prospectively to all share-based payment awards that are granted or modified on or after the effective date, or (2) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. Earlier application is

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INTERLINK ELECTRONICS, INC.

Notes to Condensed Consolidated Financial Statements - continued

(unaudited)

permitted. Effective January 1, 2016, the Company adopted ASU No. 2014-12 and it did not have a material effect on our consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, “Presentation of Financial Statements – Going Concern (Sub-Topic 205-40): Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern”, which provides guidance in GAAP about management’s responsibility to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern and to provide related footnote disclosures. This update is effective for annual periods ending after December 15, 2016 and for annual periods and interim periods thereafter. Early application is permitted. Effective January 1, 2016, the Company adopted ASU No. 2014-15 and it did not have a material effect on our consolidated financial statements.

In February 2015, the FASB issued ASU 2015-02, “Consolidation (Topic 810): Amendments to the Consolidation Analysis”, to change the analysis that a reporting entity must perform to determine whether it should consolidate certain types of legal entities. The standard is effective for fiscal and interim periods within those fiscal years, beginning after December 15, 2015. Effective January 1, 2016, the Company adopted ASU No. 2015-02 and it had no impact on our consolidated financial statements.

In November 2015, the FASB issued ASU No. 2015-17, “Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes”, which requires entities to present deferred tax assets and deferred tax liabilities as noncurrent in a classified balance sheet. The ASU may be applied prospectively or retrospectively. The Company adopted ASU 2015-17 on January 1, 2016, and applied it retrospectively.

In July 2015, the FASB issued ASU 2015-11, “Inventory (Topic 330): Simplifying the Measurement of Inventory”, which provides new guidance regarding the measurement of inventory. The new guidance requires most inventory to be measured at the lower of cost or net realizable value. The standard defines net realizable value as estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. The standard applies to companies other than those that measure inventory using last-in, first-out ("LIFO") or the retail inventory method. The standard will be effective for annual reporting periods beginning after December 15, 2016, including interim periods within those reporting periods. Early application is permitted. Effective January 1, 2017, the Company adopted ASU No. 2015-11 and it had no impact on our consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, "Compensation- Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting", which modifies and simplifies several aspects of accounting for share-based payment transactions. Changes to the current guidance primarily pertain to the income tax consequences of share-based payment transactions. Under the standard, all excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) should be recognized as income tax expense or benefit in the income statement. The tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur, regardless of whether the benefit reduces taxes payable in the current period. The full amount of excess tax benefits should be classified along with other income tax cash flows as an operating activity. When awards are settled, cash paid to the taxing authorities by an employer when directly withholding shares for tax withholding purposes will be classified as a financing activity. Additionally, with respect to forfeitures of awards, an entity can make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur. The amendments in this standard are effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods, with early adoption permitted. Effective January 1, 2017, the Company adopted ASU No. 2016-09 and it had no impact on our consolidated financial statements.

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INTERLINK ELECTRONICS, INC.

Notes to Condensed Consolidated Financial Statements - continued

(unaudited)

Recently Issued Accounting Pronouncements (Not Yet Adopted)

In May 2014, the FASB issued ASU No. 2014-09, “Revenue from Contracts with Customers (Topic 606).” The amendments to this update supersede nearly all existing revenue recognition guidance under GAAP, including the revenue recognition requirements in ASC Topic 605, “Revenue Recognition.”- The standard was originally set to become effective in annual periods beginning after December 15, 2016 and for interim and annual reporting periods thereafter. In August 2015, the FASB issued ASU 2015-14 “Revenue from Contracts with Customers; Deferral of the Effective Date,” which defers the effective date of ASU 2014-09 for all entities by one year, thereby delaying the effective date of the standard to January 1, 2018, with an option that would permit companies to adopt the standard as early as the original effective date. Early adoption prior to the original effective date is not permitted. The core principle of this Topic is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. This Topic defines a five-step process to achieve this core principle and, in doing so, it is possible more judgment and estimates may be required within the revenue recognition process than required under existing GAAP including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. The Company is currently assessing the impact of ASU 2014-09 on our consolidated financial statements to be completed by the end of 2017.

In January 2016, the FASB issued ASU No. 2016-01, “Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities”, that amends existing guidance around classification and measurement of certain financial assets and liabilities. Changes to the current GAAP model primarily affect the accounting for equity investments, financial liabilities under the fair value option, and the presentation and disclosure requirements for financial instruments. Under the new guidance, all equity investments in unconsolidated entities (other than those accounted for using the equity method of accounting) will generally be measured at fair value through earnings. For equity investments without readily determinable fair values, the cost method is also eliminated. However, most entities will be able to elect to record equity investments without readily determinable fair values at cost, less impairment, and plus or minus subsequent adjustments for observable price changes. The standard also requires that financial assets and liabilities be disclosed separately in the notes to the financial statements based on measurement principle and form of financial asset. The amendments in this guidance are effective for financial statements issued for interim and annual periods beginning after December 15, 2017. This standard is not expected to have a significant impact on our consolidated financial statements or disclosures.

In February 2016, the FASB issued ASU No. 2016-02, “Leases (Topic 842)”, which replaces the existing guidance in ASC Topic 840, “Leases”. The new standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years and requires retrospective application. The Company is currently evaluating the impact of ASU 2016-02 to our consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, “Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments”, that significantly changes how entities will measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income, including trade receivables. The standard requires an entity to estimate its lifetime “expected credit loss” for such assets at inception, and record an allowance that, when deducted from the amortized cost basis of the financial asset, presents the net amount expected to be collected on the financial asset. The standard is effective for annual periods beginning after December 15, 2019, and interim periods therein. Early adoption is permitted for annual periods beginning after December 15, 2018, and interim periods therein. This standard is not expected to have a significant impact on our consolidated financial statements or disclosures.

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INTERLINK ELECTRONICS, INC.

Notes to Condensed Consolidated Financial Statements - continued

(unaudited)

In August 2016, the FASB issued ASU No. 2016-15, “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payment,” which clarifies how cash receipts and cash payments in certain transactions are presented and classified in the statement of cash flows. The effective date of this update is for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017, with early adoption permitted. The update requires retrospective application to all periods presented but may be applied prospectively if retrospective application is impracticable. The Company has not yet evaluated the impact of the adoption of this accounting standard on our consolidated financial statements.

In October 2016, the FASB issued ASU No. 2016-16, “Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory,” which reduces the complexity in the accounting standards by allowing the recognition of current and deferred income taxes for an intra-entity asset transfer, other than inventory, when the transfer occurs. Historically, recognition of the income tax consequence was not recognized until the asset was sold to an outside party. This amendment should be applied on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. ASU 2016-16 is effective for annual periods beginning after December 15, 2017, including interim reporting periods within those annual reporting periods. Early adoption is permitted for all entities as of the beginning of an annual reporting period for which financial statements (interim or annual) have not been issued or made available for issuance. We are currently evaluating the impact of ASU 2016-16 on our consolidated financial statements and related disclosures.

In November 2016, the FASB issued ASU 2016-18, “Statement of Cash Flows (Topic 230): Restricted Cash”. The amendments in this update apply to all entities that have restricted cash or restricted cash equivalents and are required to present a statement of cash flows under Topic 230. The amendments in this Update require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. These amounts should be included within cash and cash equivalents when reconciling the beginning and ending balances for the periods shown on the statement of cash flows. The ASU requires retrospective application, and is effective for annual periods beginning after December 15, 2017, and interim periods within those annual periods. Early adoption is permitted. The Company does not expect the adoption of this accounting standard to have a material impact on our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-01, “Business Combinations (Topic 805): Clarifying the Definition of a Business”, clarifying the definition of a business, reducing the number of transactions that need to be further evaluated and providing a framework to assist entities in evaluating whether both an input and a substantive process are present. The amendments in the ASU specify that when the fair value of the gross assets acquired or disposed of is concentrated in a single identifiable asset or a group of similar identifiable assets, the integrated set of assets and activities is not a business. The guidance also requires that an integrated set of assets and activities must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output to be considered a business, and removes the evaluation of whether a market participant could replace the missing elements. The ASU is effective for annual periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019, with early adoption permitted. The Company does not expect the adoption of this accounting standard to have a material impact on our consolidated financial statements.

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INTERLINK ELECTRONICS, INC.

Notes to Condensed Consolidated Financial Statements - continued

(unaudited)

NOTE 2-INVENTORIES

Inventories, stated at the lower of cost or market, consist of the following:

	June 30, 2017	December 31, 2016
Inventories	(in thousands)	
Raw materials	$ 903	$ 738
Work-in-process	273	357
Finished goods	185	173
Total inventories	$ 1,361	$ 1,268

NOTE 3-STOCKHOLDERS' EQUITY

On April 1, 2016, we completed a stock dividend of one quarter (¼) of one share of common stock for every one (1) share of common stock outstanding. All share amounts, exercise prices, and weighted-average grant date fair value for our common stock, stock options and restricted stock reflect the stock dividend.

NOTE 4-STOCK BASED COMPENSATION

Under the terms of our 2016 Omnibus Incentive Plan (the "2016 Plan"), officers and key employees could be granted restricted stock units, as well as non-qualified or incentive stock options, at the discretion of the Compensation Committee of the Board of Directors. The Plan replaces the 1996 Stock Incentive Plan (the "1996 Plan") which was terminated in December 2015; however, all grants issued under the 1996 Plan prior to its termination will continue to vest, expire or terminate in accordance with the 1996 Plan document and the terms of each award.

Restricted Stock Units

Our outstanding restricted stock unit grants vest over five years in installments of 50% on the fourth anniversary of the grant date and the remaining 50% on the fifth anniversary of the grant date. Unvested restricted shares are forfeited if the recipient's employment terminates for any reason other than death, disability or special circumstances as determined by the Compensation Committee of the Board of Directors.

Activity for our restricted stock units is as follows:

	Restricted Stock Units (in thousands)	Weighted-Average Grant Date Fair Value	Weighted Average Remaining Contractual Life (years)	Aggregate Intrinsic Value (in thousands)
Restricted stock units, December 31, 2016	165	$ 3.54	2.33	$ 1,158
Awarded	5	$ 8.81		
Released	—	$ —		
Forfeited	(5)	$ 11.09		
Restricted stock units, June 30, 2017	165	$ 3.54	1.86	$ 1,320

The aggregate intrinsic values in the preceding table for the restricted stock units outstanding represent the total pretax intrinsic value, based on our closing stock price of $8.00 and $7.02 as of June 30, 2017 and December 31, 2016, respectively. No restricted stock units vested in the six months ended June 30, 2017.

INTERLINK ELECTRONICS, INC.

Notes to Condensed Consolidated Financial Statements - continued

(unaudited)

Stock based compensation incurred for the three and six months ended June 30, 2017 was $21 thousand and $50 thousand, respectively as compared to $18 thousand and $43 thousand for the comparable periods ended June 30, 2016.

Stock Options

The exercise price of our stock options is the closing price on the date the options are granted. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. Options generally expire 10 years from the date of grant. The following table summarizes the activity for the remaining options outstanding under the Plan:

	Shares (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (years)	Aggregate Intrinsic Value (in thousands)
Options outstanding, December 31, 2016	11	$ 3.75	0.65	$ 37
Granted	—	$ —		
Exercised	(6)	$ 4.96		
Cancelled or expired	(1)	$ 4.80		
Options outstanding, June 30, 2017	4	$ 1.56	0.77	$ 26
Options exercisable, June 30, 2017	4	$ 1.56	0.77	$ 26

This intrinsic value represents the excess of the fair market value of our common stock on the date of exercise over the exercise price of such options. The aggregate intrinsic values in the preceding table for the options outstanding represent the total pretax intrinsic value, based on our closing stock price of $8.00 and $7.02 as of June 30, 2017 and December 31 2016, respectively, which would have been received by the option holders had those option holders exercised their in-the-money options as of those dates.

The fair value of stock-based option awards is estimated at the date of grant using the Black-Scholes option pricing model; however, the value calculated using an option pricing model may not be indicative of the fair value observed in a willing buyer/willing seller market transaction, or actually realized by the employee upon exercise. Expected volatility used to estimate the fair value of options granted is based on the historical volatility of our common stock. The risk-free interest rate is based on the United States Treasury constant maturity rate for the expected life of the stock option. The expected life of a stock award is the period of time that the award is expected to be outstanding. We have not granted any stock options since 2008.

The following table provides additional information in regards to options outstanding as of June 30, 2017:

	Options Outstanding			Options Exercisable	
Range of Exercise Price	Number Outstanding (in thousands)	Weighted Average Remaining Contractual Life (years)	Weighted Average Exercise Price	Number Exercisable (in thousands)	Weighted Average Exercise Price
$ 1.56	4	0.77	$ 1.56	4	$ 1.56

NOTE 5-EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income for the period by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed by dividing net income for the period by the weighted average number of common shares outstanding during the period, plus the dilutive effect of outstanding stock options and restricted stock-based awards using the treasury stock method.

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INTERLINK ELECTRONICS, INC.

Notes to Condensed Consolidated Financial Statements - continued

(unaudited)

The following table sets forth the computation of basic and diluted earnings per share:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
	(in thousands, except per share data)			
Net income	$ 549	$ 749	$ 913	$ 1,355
Comprehensive income	$ 574	$ 724	$ 949	$ 1,334
Weighted average outstanding shares of common stock	7,333	7,326	7,331	7,326
Dilutive potential common shares from stock options and restricted stock units	87	80	85	74
Common stock and common stock equivalents	7,420	7,406	7,416	7,400
Earnings per share, basic and diluted	$ 0.07	$ 0.10	$ 0.12	$ 0.18
Comprehensive income per share: basic and diluted	$ 0.08	$ 0.10	$ 0.13	$ 0.18
Shares subject to anti-dilutive stock options and restricted stock-based awards excluded from calculation	82	87	84	93

NOTE 6-SIGNIFICANT CUSTOMERS, CONCENTRATION OF CREDIT RISK AND GEOGRAPHIC INFORMATION

We manage and operate our business through one operating segment.

Net revenues from customers equal to, or greater than, 10% of total net revenues are as follows:

	Three months ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
Customer A	25%	20 %	21%	20 %
Customer B	15%	12 %	15%	10 %
Customer C	11%	12 %	11%	11 %
Customer D	* %	14 %	* %	13 %
Customer E	* %	10 %	* %	10 %

*Less than 10% of total net revenues

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INTERLINK ELECTRONICS, INC.

Notes to Condensed Consolidated Financial Statements - continued

(unaudited)

Net revenues by geographic area are as follows:

	Three months ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
	(in thousands)		(in thousands)	
United States	$ 1,763	$ 1,913	$ 2,989	$ 3,492
Asia and Middle East	1,167	632	2,324	1,317
Europe and other	334	509	835	1,050
Revenue, net	$ 3,264	$ 3,054	$ 6,148	$ 5,859

Revenues by geographic area are based on the country of shipment destination. The geographic location of distributors and third-party manufacturing service providers may be different from the geographic location of the purchasers and/or ultimate end users.

We provide credit only to creditworthy third parties who are subject to our credit verification procedures. Accounts receivable balances are monitored on an ongoing basis, and accounts deemed to have credit risk are fully reserved. At June 30, 2017, two customers accounted for 42% and 25% of total accounts receivable, respectively. At December 31, 2016, two customers accounted for 44% and 15% of total accounts receivable, respectively. Our allowance for doubtful accounts was $0 at both June 30, 2017 and December 31, 2016.

Our long-lived assets (property, plant and equipment plus intangibles, net) were geographically located as follows:

	June 30, 2017	December 31, 2016
	(in thousands)	
United States	$ 97	$ 87
Asia	231	267

Total long-lived assets	$ 328	$ 354

NOTE 7-RELATED PARTY TRANSACTIONS

BKF Capital Group (OTC:BKFG)

We entered into an agreement, dated March 1, 2015 with BKF Capital Group, Inc. (“BKF”). Pursuant to the agreement, BKF occupies and uses one furnished office, telephone and other services, located at our corporate offices, for a fee of $1,000 per month. As of February 1, 2017 this agreement was modified as BKF relocated and no longer occupied the furnished office. Accordingly, the fee was reduced to $250 per month. In addition, we will occasionally pay administrative expenses on behalf of BKF, and BKF will reimburse the Company. For the three months ended June 30, 2017 and 2016, BKF paid $750 and $3,000, respectively to the Company. For the six months ended June 30, 2017 and 2016, BKF paid $2,250 and $6,000, respectively to the Company. Steven N. Bronson, our Chairman of the Board, President and Chief Executive Officer, is also the Chairman of the Board, Chief Executive Officer and majority shareholder of BKF. At June 30, 2017 and December 31, 2016, there were no unpaid amounts owed by BKF to us.

Qualstar Corporation (NASDAQ:QBAK)

The Company agreed to reimburse, or be reimbursed by, Qualstar Corporation (“Qualstar”) for our occupation and use of a portion of their Simi Valley manufacturing location and other expenses paid by one company on behalf of the other.

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INTERLINK ELECTRONICS, INC.

Notes to Condensed Consolidated Financial Statements - continued

(unaudited)

Steven N. Bronson, our Chairman of the Board, President and Chief Executive Officer, is also the President and Chief Executive Officer of Qualstar. Transactions with Qualstar are as follows:

	Three months ended June 30,			
	2017		2016	
	Due from Qualstar	Due to Qualstar	Due from Qualstar	Due to Qualstar
	(in thousands)			
Balance at March 31,	$ —	$ 1	$ —	$ 4
Billed to Qualstar by Interlink	1	—	4	—
Paid by Qualstar to Interlink	(1)	—	—	—
Billed to Interlink by Qualstar	—	3	—	9
Paid by Interlink to Qualstar	—	(3)	—	(10)
Balance at June 30,	$ —	$ 1	$ 4	$ 3

	Six months ended June 30,			
	2017		2016	
	Due from Qualstar	Due to Qualstar	Due from Qualstar	Due to Qualstar
	(in thousands)			
Balance at January 1,	$ 2	$ 1	$ —	$ 6
Billed to Qualstar by Interlink	7	—	6	—
Paid by Qualstar to Interlink	(9)	—	(2)	—
Billed to Interlink by Qualstar	—	5	—	20
Paid by Interlink to Qualstar	—	(5)	—	(23)
Balance at June 30,	$ —	$ 1	$ 4	$ 3

NOTE 8-INCOME TAXES

Income tax expense as a percentage of income before income taxes was 33.4% and 34.2% for the three and six months ended June 30, 2017 versus 19.4% and 13.2% for the comparable period in the prior year. Our income tax expense is primarily impacted by the mix of domestic and foreign pre-tax earnings, as well as our ability to utilize prior net operating loss carryovers (“NOLs”).

The Company experienced an ownership change under IRC Section 382 in February 2010. In general, a Section 382 ownership change occurs if there is a cumulative change in our ownership by “5% shareholders” (as defined in the Internal Revenue Code of 1986, as amended) that exceeds 50 percentage points over a rolling three-year period. An ownership change generally affects the rate at which NOLs and potential other deferred tax assets are permitted to offset future taxable income. Certain state jurisdictions within which we operate contain similar provisions and limitations. All of the remaining federal and state NOLs as of June 30, 2017 are subject to annual limitations due to the February 2010 ownership change.

Management assesses the available positive and negative evidence to estimate if sufficient future taxable income will be generated to utilize the existing deferred tax assets. We analyzed our need to maintain the valuation allowance against

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INTERLINK ELECTRONICS, INC.

Notes to Condensed Consolidated Financial Statements - continued

(unaudited)

our otherwise recognizable deferred tax assets in the federal, state and foreign jurisdictions and had previously recorded a full valuation allowance. During the fourth quarter of 2016, we determined, given our current earnings and anticipated future earnings, that sufficient evidence existed to reach a conclusion that the valuation allowance was no longer warranted.

NOTE 9-COMMITMENTS AND CONTINGENCIES

Operating Leases

We lease certain facilities under non-cancellable operating leases. The leases expire at various dates through fiscal 2021 and frequently include renewal provisions for varying periods of time, provisions which require us to pay taxes, insurance and maintenance costs, and provisions for minimum rent increases. Minimum lease payments, including scheduled rent increases are recognized as rent expenses on a straight-line basis over the term of the lease.

Future minimum lease payments under non-cancellable operating leases that have remaining non-cancellable lease terms in excess of one year are as follows:

	Remaining 2017	2018	2019	2020	Thereafter	Total
	(in thousands)					
Operating Leases	$ 141	$ 226	$ 183	$ 120	$ 68	$ 738

Litigation

We are not party to any legal proceedings at June 30, 2017. We are occasionally involved in legal proceedings in the ordinary course of business, including actions against us which assert or may assert claims or seek to impose fines and penalties in substantial amounts. Related legal defense costs are expensed as incurred.

Warranties

We establish reserves for future product warranty costs that are expected to be incurred pursuant to specific warranty provisions with our customers. We generally warrant our products against defects for one year from date of shipment, with certain exceptions in which the warranty period can extend to more than one year based on contractual agreements. Our warranty reserves are established at the time of sale and updated throughout the warranty period based upon numerous factors including historical warranty return rates and expenses over various warranty periods. Historically, our warranty returns have not been material.

Intellectual Property Indemnities

We indemnify certain customers and our contract manufacturers against liability arising from third-party claims of intellectual property rights infringement related to our products. These indemnities appear in development and supply agreements with our customers as well as manufacturing service agreements with our contract manufacturers, are not limited in amount or duration and generally survive the expiration of the contract. Given that the amount of any potential liabilities related to such indemnities cannot be determined until an infringement claim has been made, we are unable to determine the maximum amount of losses that we could incur related to such indemnifications.

Director and Officer Indemnities and Contractual Guarantees

We have entered into indemnification agreements with our directors and executive officers, which require us to indemnify such individuals to the fullest extent permitted by Nevada law. Our indemnification obligations under such agreements are not limited in amount or duration. Certain costs incurred in connection with such indemnifications may

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Notes to Condensed Consolidated Financial Statements - continued

(unaudited)

be recovered under certain circumstances under various insurance policies. Given that the amount of any potential liabilities related to such indemnities cannot be determined until a lawsuit has been filed, we are unable to determine the maximum amount of losses that we could incur relating to such indemnities.

We have also entered into an employment agreement with Steven N. Bronson, our Chairman of the Board, President and Chief Executive Officer. This agreement contains certain severance and change in control obligations. Under the agreement, if Mr. Bronson's employment is terminated due to his death or disability (as such terms are defined in the agreement), Mr. Bronson or his beneficiaries will be entitled to receive: (i) his base compensation to the end of the monthly pay period immediately following the date of termination; (ii) accrued bonus payments; and (iii) all unvested equity and/or options issued by the Company shall immediately fully vest. If Mr. Bronson's employment is terminated by him for good reason (as such term is defined in the agreement), or by us without cause, then Mr. Bronson will be entitled to receive: (i) his base compensation to the date of termination; (ii) a severance payment equal to twelve months of his base compensation; (iii) any earned bonus compensation; (iv) employee benefits for twelve months following the date of termination; (v) any vested company match 401k or other retirement contribution; and (vi) all unvested equity and/or options issued by the Company shall immediately fully vest.

In the event of a change in control of the Company (as such term is defined in the agreement), Mr. Bronson is entitled to receive: (i) a change in control payment in an amount equal to twelve months of his base compensation, payable as of the date the change in control occurs; and (ii) all unvested equity and/or options issued by the Company shall immediately fully vest.

Guarantees and Indemnities

In the normal course of business, we are occasionally required to undertake indemnification for which we may be required to make future payments under specific circumstances. We review our exposure under such obligations no less than annually, or more frequently as required. The amount of any potential liabilities related to such obligations cannot be accurately determined until a formal claim is filed. Historically, any such amounts that become payable have not had a material negative effect our business, financial condition or results of operations. We maintain general and product liability insurance which may provide a source of recovery to us in the event of an indemnification claim.

NOTE 10-SUBSEQUENT EVENT

None.

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

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The words “believe,” “may,” “will,” “potentially,” “estimate,” “continue,” “anticipate,” “intend,” “could,” “would,” “project,” “plan,” “ex expressions that convey uncertainty of future events or outcomes are intended to identify forward-looking statements. These forward-looking statements include, but are not limited to, statements concerning the following:

- our future financial and operating results;
- our business strategy;
- our intentions, expectations and beliefs regarding anticipated growth, market penetration and trends in our business;
- our dependence on growth in our customers’ businesses;
- the effects of market conditions on our stock price and operating results;
- our ability to maintain our competitive technological advantages against competitors in our industry;
- our ability to timely and effectively adapt our existing technology and have our technology solutions gain market acceptance;
- our ability to introduce new products and bring them to market in a timely manner;
- our ability to maintain, protect and enhance our intellectual property;
- the effects of increased competition in our market and our ability to compete effectively;
- costs associated with defending intellectual property infringement and other claims;
- our expectations concerning our relationships with customers and other third parties;

- our expectations concerning relationships between our customers and their manufacturers;

- the attraction and retention of qualified employees and key personnel;

- future acquisitions of or investments in complementary companies or technologies; and

- our ability to comply with evolving legal standards and regulations, particularly concerning requirements for being a public company and United States export regulations.

These forward-looking statements speak only as of the date of this Form 10-Q and are subject to uncertainties, assumptions and business and economic risks. As such, our actual results could differ materially from those set forth in the forward-looking statements as a result of the factors set forth below in Part II, Item 1A, "Risk Factors," and in our other reports filed with the Securities and Exchange Commission. Moreover, we operate in a very competitive and rapidly changing environment, and new risks emerge from time to time. It is not possible for us to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In light of these risks, uncertainties and assumptions, the forward-looking events and circumstances discussed in this Form 10-Q may not occur, and actual results could differ materially and adversely from those anticipated or implied in our forward-looking statements.

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You should not rely upon forward-looking statements as predictions of future events. Although we believe that the expectations reflected in our forward-looking statements are reasonable, we cannot guarantee that the future results, levels of activity, performance or events and circumstances described in the forward-looking statements will be achieved or occur. Moreover, neither we nor any other person assumes responsibility for the accuracy and completeness of the forward-looking statements. We undertake no obligation to update publicly any forward-looking statements for any reason after the date of this Form 10-Q to conform these statements to actual results or to changes in our expectations, except as required by law.

The following discussion should be read in conjunction with our unaudited condensed consolidated financial statements and notes thereto appearing elsewhere in this Quarterly Report on Form 10-Q with the understanding that our actual future results, levels of activity, performance and events and circumstances may be materially different from what we expect.

Overview and Outlook

Overview

Interlink Electronics, Inc. ("we", "us", "our", "Interlink" or the "Company") designs, develops, manufactures and sells a range force-sensing technologies that incorporate our proprietary materials technology, firmware and software into a portfolio of standard products and custom solutions. These include sensor components, subassemblies, modules and products that support effective, efficient cursor control and novel three-dimensional user inputs. Our Human Machine Interface ("HMI") technology platforms are deployed in a wide range of markets including consumer electronics, automotive, industrial, and medical. The application of our HMI technology platforms includes vehicle entry, vehicle multi-media control interface, rugged touch controls, presence detection, collision detection, speed and torque controls, biological monitoring and others.

Interlink has been a leader in the printed electronics industry for 30 years with the commercialization of our patented Force Sensing Resistor ("FSR®") technology that has enabled rugged and reliable HMI solutions. Our solutions have focused on handheld user input, menu navigation, cursor control, and other intuitive interface technologies for the world's top electronics manufacturers.

We sell our products globally to a diverse array of customers that include the Fortune 500 as well as start-ups, design houses, original design manufacturers, OEMs and universities. Our technology has been deployed in the consumer electronics, industrial automation, automotive and medical markets. Our global presence in the United States, China, Hong Kong, Singapore and Japan, allows us to provide local sales and engineering support services to our existing and future customers. Our products are manufactured by our wholly-owned subsidiary in a state-of-the-art facility in Shenzhen, China. We also maintain engineering, assembly and prototyping capabilities in Simi Valley, California. We control 100% of the manufacturing and shipping process which enables us to respond quickly to customer product demand and design requirements.

Over the next three-to-five years, we anticipate investing significantly in the expansion of our technology platforms through our own internal development to ensure we provide the market with leading-edge HMI solutions that are seamless to deploy and preform flawlessly. We anticipate dramatically growing our R&D organization in Singapore to ensure we have the right team to launch our current designs and develop new product offerings that will meet the market's growing demand for touch technology. Our Singapore location will allow us to take advantage of the abundance of engineering talent for future new product development. We also plan to explore potential strategic relationships with Singapore-based companies and technology institutes that will support our growth initiatives.

Outlook

We follow market research conducted by IDTechEx and other independent parties in the printed, flexible electronics industry. Market research indicates that the sensor portion of the printed electronics market is a $6.5 billion industry and continues to grow. We maintain our focus on developing solutions around scalable sensor and product architectures and emerging applications in order to capitalize on this growth. We believe there are significant innovation opportunities for sensors with novel functions and form factors, which is why we have invested heavily in R&D to develop disruptive

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technology platforms and a robust patent portfolio. We expect to accelerate such investments over the next 12 – 18 months as we continue to build out our R&D engineering center in Singapore.

The industrial markets we serve (automotive, medical, rugged computing, industrial tools and equipment, among others) face challenges driven by product innovation, changes in talent requirements, and disruptions in energy markets. Such challenges present an opportunity for us to emerge as a solution provider for these markets. These opportunities include: new technologies such as industrial IoT, robotics and advanced manufacturing, and the skills and solutions needed to manage embedded technology and data analytics. If capitalized and managed correctly, these innovations can support step changes in productivity by allowing companies to more actively monitor and optimize plant, asset, and supply chain performance.

The consumer market faces an unprecedented confluence of changes such as declining brand loyalty, rapidly evolving technologies, changing demographics and consumer preferences, and economic uncertainty. The opportunities for us are to provide solutions to help consumer products companies keep up with the frantic pace of innovation to maintain performance of existing categories while also building the breakthrough new businesses of the future. The advent of smarter products (e.g., products with embedded sensor technologies) provides an opportunity for us to deliver unique solutions to build and nurture breakthrough innovation.

Overall, our customers tend to be market leaders, and have been stable enough to manage their businesses through any challenging market cycle. We are very pleased with our performance in the three and six months ended June 30, 2017. We are confident that our leadership position in providing HMI solutions remains strong.

Our effective tax rate is directly impacted by the relative proportions of revenue and income before taxes in the jurisdictions in which we operate. Unusual or discrete tax events may cause our effective rate to fluctuate on a quarterly basis. Certain events, including, for example, acquisitions and other business changes, which are difficult to predict, may also cause our effective tax rate to fluctuate. We are subject to changing tax laws, regulations, and interpretations in multiple jurisdictions. Corporate tax reform continues to be a priority in the U.S. and other jurisdictions. Changes to the tax system in the U.S. could have significant effects, positive and negative, on our effective tax rate, and on our deferred tax assets and liabilities.

We remain committed to our strategy to create shareholder value through earnings growth and balanced capital allocation, including disciplined investments for organic growth and innovation and strategic bolt-on acquisitions. In connection with our growth strategy, we will continue to evaluate potential acquisitions in 2017; however, the effect of such acquisitions cannot be predicted and therefore is not reflected in this outlook.

Critical Accounting Policies and Estimates

The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions about future events that affect the amounts reported in the condensed consolidated financial statements and accompanying notes to the condensed consolidated financial statements. Actual results could differ significantly from those estimates. We base our estimates on historical experience and on various other assumptions that we believe are reasonable in the circumstances. We regularly discuss with our audit committee the basis of our estimates. These estimates could change under different assumptions or conditions.

We believe that our critical accounting polices and estimates, as described in our annual Report on Form 10-K for the year ended December 31, 2016, are most important to the portrayal of our financial condition and results of operations and require management's most difficult, subjective and complex judgments. There have been no significant changes to these polices during the six months ended June 30, 2017.

Impact of Recent Accounting Pronouncements

For information with respect to recent accounting pronouncements and the impact of these pronouncements see "Note 1 - The Company and its Significant Accounting Policies – Recently Adopted Accounting Pronouncements" and "Recently Issued Acconting Pronouncements (Not Yet Adopted)" in the accompanying notes to the unaudited condensed consolidated financial statements.

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Results of Operations

The following table sets forth certain unaudited condensed consolidated statements of income data for the periods indicated. The percentages in the table are based on net revenues.

	Three months ended June 30,				Six months ended June 30,			
	2017		2016		2017		2016	
	$	%	$	%	$	%	$	%
	(in thousands, except percentages)							
Revenue, net	$ 3,264	100.0 %	$ 3,054	100.0 %	$ 6,148	100.0 %	$ 5,859	100.0 %
Cost of revenue	1,203	36.9 %	1,211	39.7 %	2,351	38.2 %	2,345	40.0 %
Gross profit	2,061	63.1 %	1,843	60.3 %	3,797	61.8 %	3,514	60.0 %
Operating expenses:								
Engineering, research and development	157	4.8 %	174	5.7 %	335	5.4 %	315	5.4 %
Selling, general and administrative	1,065	32.6 %	755	24.7 %	2,092	34.1 %	1,667	28.5 %
Total operating expenses	1,222	37.4 %	929	30.4 %	2,427	39.5 %	1,982	33.9 %
Income from operations	839	25.7 %	914	29.9 %	1,370	22.3 %	1,532	26.1 %
Other income (expense):								
Other income (expense), net	(2)	(0.1) %	15	0.5 %	17	0.3 %	29	0.5 %
Income before income tax expense	837	25.6 %	929	30.4 %	1,387	22.6 %	1,561	26.6 %
Income tax expense	288	8.8 %	180	5.9 %	474	7.7 %	206	3.5 %
Net income	549	16.8 %	749	24.5 %	913	14.9 %	1,355	23.1 %
Other comprehensive income, net of tax:								
Foreign currency translation	25	0.8 %	(25)	(0.8) %	36	0.5 %	(21)	(0.3) %

adjustments								
Comprehensive income	$ 574	17.6 %	$ 724	23.7 %	$ 949	15.4 %	$ 1,334	22.8 %

Results of Operations for the three months ended June 30, 2017, as compared to the three months ended June 30, 2016

Revenue, net by Market is as follows:

	Three months ended June 30,					
	2017		2016			
	Amount	% of Net Revenue	Amount	% of Net Revenue	Change	% Change
	(in thousands, except percentages)					
Automotive	$ 1,016	31.1 %	$ 920	30.1 %	$ 96	10.4 %
Industrial	475	14.5 %	313	10.2 %	162	51.7 %
Medical	350	10.7 %	361	11.8 %	(11)	(3.0) %
Consumer	486	14.9 %	367	12.0 %	119	32.5 %
Standard	937	28.8 %	1,093	35.9 %	(156)	(14.2) %
Revenue, net	$ 3,264	100.0 %	$ 3,054	100.0 %	$ 210	6.9 %

We sell our custom products into the following markets: automotive, industrial, medical and consumer. We sell our standard products in many different markets which are often unknown to us at the time of sale. Each market has different product design cycles. Products with longer design cycles often have much longer product life-cycles. Automotive, industrial, and medical products generally have longer design and life-cycles than consumer products. We currently have products with life-cycles that have exceeded twenty years and are ongoing.

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The increase in net revenues was driven by increased sales of our custom products in the industrial, automotive and consumer markets, partially offset by decreased sales of our custom products into the medical market. We also had a significant decrease in sales of our standard products. The overall growth in our custom product sales was driven by increased sales to our current customers for use in ongoing product lines. Some of our larger customers purchase product in bulk quantities and absorption of these products can straddle several financial reporting periods. The timing of orders from our customers is not always predictable and can be concentrated in varying periods during the year to coincide with their project and building plans.

Some of our more recent custom product success for new product lines in the automotive and medical markets will not be realized until late 2017 or early 2018. However, as these revenues materialize, revenues from current product lines that reach the end of their life cycle will likely offset some of this expected growth.

We anticipate sales of custom products into the automotive market, and total revenues, for the second half of 2017 to be lower as compared to the comparable period of 2016, due to a major customer’s design change eliminating the need for our soulution.

	Three months ended June 30,								
	2017			2016					
	Amount	% of Net Revenue		Amount	% of Net Revenue		Change	% Change	
	(in thousands, except percentages)								
Cost of revenue	$ 1,203	36.9	%	$ 1,211	39.7	%	$ (8)	(0.7)	%

Our cost of revenue is impacted by various factors including product mix, volume, material costs, manufacturing efficiencies, facilities costs, compensation costs and any provisions for excess and obsolete inventories. Cost of revenues was flat compared with the same period in the prior year despite our increase in revenues. Cost of revenues decreased as a percentage of revenues primarily due to efficiencies gained, including improved utilization of fixed costs and other production overhead costs, as revenues increased.

	Three months ended June 30,								
	2017			2016					
	Amount	% of Net Revenue		Amount	% of Net Revenue		Change	% Change	
	(in thousands, except percentages)								
Engineering, research and development	$ 157	4.8	%	$ 174	5.7	%	$ (17)	(9.8)	%

Engineering and R&D expenses consist primarily of compensation expenses for employees engaged in research, design and development activities. Our R&D team focuses both on internal design development, as well as design development aimed at addressing customer design challenges, in order to develop our HMI solutions.

Our engineering and R&D costs decreased as compared with the same period in the prior year primarily due to the timing of investment in our Singapore R&D center. We intend to continue to grow the global R&D center in Singapore substantially over the next three-to-five years, including expanding our R&D team, expanding the size of the facility, and investing in additional tools and equipment. On February 24, 2016, we entered into a five-year lease agreement for a new R&D facility in Singapore and moved into the new facility in July 2016.

	Three months ended June 30,								
	2017			2016					
	Amount	% of Net Revenue		Amount	% of Net Revenue		Change	% Change	
	(in thousands, except percentages)								
Selling, general and administrative	$ 1,065	32.6	%	$ 755	24.7	%	$ 310	41.1	%

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Selling, general and administrative expenses ("SG&A") consist primarily of compensation expenses, legal and other professional fees, facilities expenses and communication expenses. SG&A expenses increased as compared with the same period in the prior year driven by increased costs related to realigning our sales and marketing strategy. We added a Vice President of Sales and Marketing in August 2016 and have made other sales related resource investments in order to focus efforts on reaching a larger share of the markets we serve.

	Three months ended June 30,								
	2017			2016					
	Amount	% of Pre-tax Income		Amount	% of Pre-tax Income		Change	% Change	
	(in thousands, except percentages)								
Income tax benefit (expense)	$ 288	34.4	%	$ 180	19.4	%	$ 108	60.0	%

Tax expense for the three months ended June 30, 2017 reflects statutory tax rates in the jurisdictions that we operate adjusted for normal book/tax differences. Tax expense for the three months ended June 30, 2016 was substantially reduced by net operating loss ("NOL") carryovers for which no prior benefit was taken. Because of the change of ownership provisions of the Tax Reform Act of 1986, use of a portion of our domestic NOL and tax credit carryforwards is limited in future periods. Further, a portion of the carryforwards may expire before being applied to reduce future income tax liabilities. As a result, we had recorded a valuation allowance against all of our net deferred tax assets. During the fourth quarter of 2016, we determined, given our current earnings and anticipated future earnings, that sufficient evidence existed to reach a conclusion that the valuation allowance will no longer be needed.

Results of Operations for the six months ended June 30, 2017, as compared to the six months ended June 30, 2016

Revenue, net by Market is as follows:

	Six months ended June 30,								
	2017			2016					
	Amount	% of Net Revenue		Amount	% of Net Revenue		Change	% Change	
	(in thousands, except percentages)								
Automotive	$ 1,716	27.9	%	$ 1,726	29.5	%	$ (10)	(0.6)	%
Industrial	1,121	18.2	%	808	13.8	%	313	38.8	%
Medical	698	11.4	%	662	11.3	%	36	5.5	%

Consumer		935	15.2	%		610	10.4	%		325	53.2	%
Standard		1,677	27.3	%		2,053	35.0	%		(376)	(18.3)	%
Revenue, net	$	6,148	100.0	%	$	5,859	100.0	%	$	289	4.9	%

The increase in net revenues was driven by increased sales of our custom products in the industrial and consumer markets, slightly offset by decreased sales of our custom products into the automotive market. We also had a significant decrease in sales of our standard products. The overall growth in our custom product sales was driven by increased sales to our current customers for use in ongoing product lines. Some of our larger customers purchase product in bulk quantities and absorption of these products can straddle several financial reporting periods. The timing of orders from our customers is not always predictable and can be concentrated in varying periods during the year to coincide with their project and building plans.

Some of our more recent custom product success for new product lines in the automotive and medical markets will not be realized until late 2017 or early 2018. However, as these revenues materialize, revenues from current product lines that reach the end of their life cycle will likely offset some of this expected growth.

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	Six months ended June 30,									
	2017			2016						
	Amount	% of Net Revenue		Amount	% of Net Revenue		Change		% Change	
	(in thousands, except percentages)									
Cost of revenue	$ 2,351	38.2	%	$ 2,345	40.0	%	$	6	0.3	%

Cost of revenues was flat compared with the same period in the prior year despite our increase in revenues. Cost of revenues decreased as a percentage of revenues primarily due to efficiencies gained, including improved utilization of fixed costs and other production overhead costs, as revenues increased.

	Six months ended June 30,									
	2017			2016						
	Amount	% of Net Revenue		Amount	% of Net Revenue		Change		% Change	
	(in thousands, except percentages)									
Engineering, research and development	$ 335	5.4	%	$ 315	5.4	%	$	20	6.3	%

Our engineering and R&D costs increased as compared with the same period in the prior year primarily due to the investment in our Singapore R&D center and an increase in our engineering and R&D staffing worldwide in order to enhance our technology and product offerings. We intend to continue to grow the global R&D center in Singapore substantially over the next three-to-five years, including expanding our R&D team, expanding the size of the facility, and investing in additional tools and equipment. On February 24, 2016, we entered into a five-year lease agreement for a new R&D facility in Singapore and moved into the new facility in July 2016.

	Six months ended June 30,					
	2017		2016			
	Amount	% of Net	Amount	% of Net	Change	% Change

		Revenue			Revenue				
	(in thousands, except percentages)								
Selling, general and administrative	$ 2,092	34.1	%	$ 1,667	28.5	%	$ 425	25.5	%

SG&A expenses increased significantly as compared with the same period in the prior year driven by increased costs related to realigning our sales and marketing strategy. We added a Vice President of Sales and Marketing in August 2016 and have made other sales related resource investments in order to focus efforts on reaching a larger share of the markets we serve.

	Six months ended June 30,								
	2017			2016					
	Amount	% of Pre-tax Income		Amount	% of Pre-tax Income		Change	% Change	
	(in thousands, except percentages)								
Income tax benefit (expense)	$ 474	34.2	%	$ 206	13.2	%	$ 268	130.1	%

Tax expense for the six months ended June 30, 2017 reflects statutory tax rates in the jurisdictions that we operate adjusted for normal book/tax differences. Tax expense for the six months ended June 30, 2016 was substantially reduced by net operating loss (“NOL”) carryovers for which no prior benefit was taken. Because of the change of ownership

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provisions of the Tax Reform Act of 1986, use of a portion of our domestic NOL and tax credit carryforwards is limited in future periods. Further, a portion of the carryforwards may expire before being applied to reduce future income tax liabilities. As a result, we had recorded a valuation allowance against all of our net deferred tax assets. During the fourth quarter of 2016, we determined, given our current earnings and anticipated future earnings, that sufficient evidence existed to reach a conclusion that the valuation allowance will no longer be needed.

Liquidity and Capital Resources

Cash requirements for working capital and capital expenditures have been funded from cash balances on hand and cash generated from operations. As of June 30, 2017, we had cash and cash equivalents of $7.0 million, working capital of $9.6 million and no indebtedness. Cash and cash equivalents consist of cash and money market funds. We did not have any short-term or long-term investments as of June 30, 2017. Of the $7.0 million of cash balances on hand, $1.4 million was held by foreign subsidiaries. If these funds are needed for our operations in the U.S., we have several methods to repatriate without significant tax effects, including repayment of intercompany loans or distributions of previously taxed income. Other distributions may require us to incur U.S. or foreign taxes to repatriate these funds. However, our intent is to permanently reinvest these funds outside the U.S. and our current plans do not demonstrate a need to repatriate cash to fund our U.S. operations.

We believe that our existing cash and cash equivalents balance will be sufficient to maintain our operations considering our current financial condition, obligations, and other expected cash flows for at least the next twelve months following the date these consolidated financial statements were available for issuance. We are proactively pursuing acquisition opportunities. It is possible our cash requirements for one or more acquisition opportunities could exceed our cash balance at the time of closing. If we require additional cash, we may attempt to raise additional capital through equity, equity-linked or debt financing arrangements. If we raise additional funds by issuing equity or equity-linked securities, the ownership of our existing stockholders will be diluted. If we raise additional financing by the incurrence of indebtedness, we will be subject to fixed payment obligations and could also be subject to restrictive covenants, such as limitations on our ability to incur additional debt, and other operating restrictions that could adversely impact our ability to conduct our business. If we are unable to raise additional needed funds, we may also take measures to reduce expenses to offset any shortfall.

There can be no assurances that we will be able to raise additional needed capital on acceptable terms or at all, and the failure to do so could adversely affect our ability to achieve our business objectives. In addition, if our future operating performance is below our expectations, our liquidity and ability to operate our business could be adversely affected.

Cash Flow Analysis

Our cash flows from operating, investing and financing activities are summarized as follows:

	Six months ended June 30,	
	2017	2016
	(in thousands)	
Net cash provided by operating activities	$ 949	$ 1,156
Net cash used in investing activities	$ (60)	$ (166)
Net cash provided by financing activities	$ 34	$ —

Net Cash Provided by Operating Activities

For the six months ended June 30, 2017, the $949 thousand in net cash provided by operating activities was primarily attributable to net income of $913 thousand, adjusted for non-cash charges of $136 thousand. The net decrease in cash due to changes in operating assets and liabilities of $100 thousand was primarily due to the timing of shipments and payments during the period, as discussed below.

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For the six months ended June 30, 2016, the $1.2 million in net cash provided by operating activities was primarily attributable to net income of $1.4 million and adjustments for non-cash charges of $77 thousand. This was offset by a net decrease due to changes in operating assets and liabilities of $276 thousand.

Accounts receivable slightly increased from $1.7 million at December 31, 2016 to $2.0 million at June 30, 2017 due to the timing of shipments and payments at year-end. Inventories increased from $1.3 million at December 31, 2016 to $1.4 million at June 30, 2017. Inventory balances will fluctuate at the end of any accounting period depending on the timing of materials purchases and product shipments. Accounts payable, accrued payables, accrued expenses, and other accrued liabilities decreased from $762 thousand at December 31, 2016 to $739 thousand at June 30, 2017 primarily due to the timing of payment for purchases of materials and other services provided.

Net Cash Used in Investing Activities

Net cash used in investing activities was $60 thousand for the six months ended June 30, 2017, compared to $166 thousand for the six months ended June 30, 2016. The decrease was primarily related to leasehold improvements for the expansion of our global R&D center in Singapore in the second quarter of 2016.

Net Cash Provided by Financing Activities

Proceeds from the exercising of stock options was $34 thousand and $0 for the six months ended June 30, 2017 or 2016, respectively.

Off-Balance Sheet Arrangements

At June 30, 2017 and December 31, 2016, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. As such, we are not exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

Contractual Obligations and Commercial Commitments

Indemnification Agreements

In the ordinary course of business, we enter into agreements of varying scope and terms pursuant to which we agree to indemnify customers, vendors, lessors, business partners and other parties with respect to certain matters, including, but not limited to, losses arising out of breach of such agreements, services to be provided by us or from intellectual property infringement claims made by third parties. In addition, we have entered into indemnification agreements with directors and certain officers and employees that will require us, among other things, to indemnify them against certain liabilities that may arise by reason of their status or service as directors, officers or employees. No demands have been made upon us to provide indemnification under such agreements and there are no claims that we are aware of that could have a material effect on our consolidated financial position and results of operations.

Operating Leases

We lease various office and manufacturing facilities, including our corporate headquarters in Westlake Village, California, under operating lease agreements that expire through 2021. The terms of the lease agreements provide for rental payments on a graduated basis. We recognize rent expense on a straight-line basis over the lease periods.

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Commitments

As of June 30, 2017, our principal commitments consisted of obligations under the operating leases for our office and manufacturing facilities. The following table summarizes our future minimum payments under these arrangements:

	Remaining 2017	2018	2019	2020	Thereafter	Total
	(in thousands)					
Operating Leases	$ 141	$ 226	$ 183	$ 120	$ 68	$ 738

Item 3.Quantitative and Qualitative Disclosures About Market Risk

Not Applicable.

Item 4.Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The phrase “disclosure controls and procedures” refers to controls and procedures designed to ensure that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934, as amended, or the Exchange Act, such as this Quarterly Report on Form 10-Q, is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the U.S. Securities and Exchange Commission, or SEC. Disclosure controls and procedures are also designed to ensure that such information is accumulated and communicated to our management, including our chief executive officer, or CEO, and chief financial officer, or CFO, as appropriate to allow timely decision regarding required disclosure.

Our management, with the participation of our CEO and CFO, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act), as of June 30, 2017, the end of the period covered by this Quarterly Report on Form 10-Q. Based on such evaluation, our CEO and CFO had concluded that as of June 30, 2017, our disclosure controls and procedures were designed at a reasonable assurance level and were effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the SEC, and that such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Controls over Financial Reporting

There was no change in our internal control over financial reporting during the period ended June 30, 2017 that materially affected, or is reasonable likely to materially affect, our internal control over financial reporting.

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PART II: OTHER INFORMATION

Item 1A.Risk Factors

This Quarterly Report on Form 10-Q contains forward-looking statements, which are subject to a variety of risks and uncertainties. Other actual results could differ materially from those anticipated in those forward-looking statements as a result of various factors, including those set forth in the risk factors relating to our business and common stock contained in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2016. There have been no material changes to such risk factors during the nine months ended June 30, 2017.

Item 6.Exhibits

Exhibit Number	Exhibit Description	Incorporated by Reference Form	File Number	Exhibit	Filing Date	Filed Herewith
3.1	Articles of Incorporation of the Registrant	10	000-21858	3.1	February 17, 2016	
3.2	Bylaws of the Registrant	10	000-21858	3.2	February 17, 2016	
31.1	Certification of Principal Executive Officer and Principal Financial Officer Pursuant to Securities Exchange Act Rules 13a-14(a) and 15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002					X
32.1*	Certification of Principal Executive Officer and Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of					X

	the Sarbanes-Oxley Act of 2002	
101.INS	XBRL Instance Document	X
101.SCH	XBRL Taxonomy Extension Schema Document	X
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document	X
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document	X
101.LAB	XBRL Taxonomy Extension Label Linkbase Document	X
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document	X

*The information in this exhibit is furnished and deemed not filed with the Securities and Exchange Commission for purposes of section 18 of the Exchange Act of 1934, as amended, and is not to be incorporated by reference into any filing of Interlink Electronics, Inc. under the Securities Act of 1933, as amended, or the Exchange Act of 1934, as amended, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

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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.

Date: August 10, 2017	Interlink Electronics, Inc. (Registrant)
	By: /s/ Steven N. Bronson Steven N. Bronson Chief Executive Officer, President and Chief Financial Officer (Principal Financial and Accounting Officer)