

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

*(Mark One)*

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES

EXCHANGE ACT OF 1934

For the Quarterly Period Ended January 31, 2004

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: 0-23246

**DAKTRONICS, INC.**

(Exact name of Registrant as specified in its charter)

**South Dakota**  
(State or other jurisdiction of  
incorporation or organization)

**46-0306862**  
(I.R.S. Employer  
Identification Number)



**331 32nd Avenue**  
**Brookings, SD 57006**

(Address of principal executive offices, zip code)

**(605) 697-4000**  
(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 is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).  
Yes  No

The number of shares of the registrant's common stock outstanding as of February 18, 2004 was 18,805,743.

**DAKTRONICS, INC. AND SUBSIDIARIES**  
FORM 10-Q  
For the Quarter Ended January 31, 2004

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[Ex. 10.14](#) [FOURTH AMENDMENT](#), DATED DECEMBER 2, 2003 TO THE LOAN AGREEMENT DATED OCTOBER 14, 1998 BETWEEN US BANK NATIONAL ASSOCIATION AND DAKTRONICS, INC.

[Ex. 31.1](#) [CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER](#) REQUIRED BY RULE 13a-14(a) OR RULE 15d-14 (a) OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

[Ex. 31.2](#) [CERTIFICATION OF THE CHIEF FINANCIAL OFFICER](#) REQUIRED BY RULE 13a-14(a) OR RULE 15d-14 (a) OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

[Ex. 32.1](#) [CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER](#) PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

[Ex. 32.2](#) [CERTIFICATION OF THE CHIEF FINANCIAL OFFICER](#) PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

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**Special Note Regarding Forward-Looking Statements**

*This Quarterly Report on Form 10-Q (including exhibits and information incorporated by reference herein) contains both historical and forward-looking statements that involve risks, uncertainties and assumptions. The statements contained in this report that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended including statements regarding the Company's expectations, beliefs, intentions and strategies for the future. These statements appear in a number of places in this Report and include all statements that are not historical statements of fact regarding the intent, belief or current expectations of the Company, its directors or its officers with respect to, among other things: (i) the Company's financing plans; (ii) trends affecting the Company's financial condition or results of operations; (iii) the Company's growth strategy and operating strategy; and (iv) the declaration and payment of dividends. The words "may," "would," "could," "will," "expect," "estimate," "anticipate," "believe," "intend," "plans" and similar expressions and variations thereof are intended to identify forward-looking statements. Investors are cautioned that any such forward-looking statements are not guarantees of future performance and involve risk and uncertainties, many of which are beyond the Company's ability to control, and that actual results may differ materially from those projected in the forward-looking statements as a result of various factors discussed herein and those factors discussed in detail in the Company's filings with the Securities and Exchange Commission.*

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**PART I. FINANCIAL INFORMATION**

**Item 1. FINANCIAL STATEMENTS**

**DAKTRONICS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
(in thousands, except per share data)

|                           | January 31,<br>2004<br>(unaudited) | May 3,<br>2003<br>(note 1) |
|---------------------------|------------------------------------|----------------------------|
| <b>ASSETS</b>             |                                    |                            |
| CURRENT ASSETS:           |                                    |                            |
| Cash and cash equivalents | \$ 10,027                          | \$ 9,277                   |

|  |           |           |
|--|-----------|-----------|
| Accounts receivable, less allowance for doubtful accounts<br>of \$1,203 at January 31, 2004 and \$1,102 at May 3, 2003 | 27,927    | 25,912    |
| Current maturities of long-term receivables  | 3,693     | 2,650     |
| Inventories  | 18,004    | 14,863    |
| Costs and estimated earnings in excess of billings   | 14,111    | 11,467    |
| Prepaid expenses and other   | 858       | 756       |
| Deferred income taxes  | 4,151     | 3,801     |
|  | <hr/>     | <hr/>     |
| Total current assets   | 78,771    | 68,726    |
|  | <hr/>     | <hr/>     |
| Advertising rights, net  | 636       | 385       |
| Long term receivables, less current maturities   | 11,591    | 6,711     |
| Goodwill, net of accumulated amortization  | 1,083     | 1,043     |
| Intangible and other assets  | 866       | 873       |
|  | <hr/>     | <hr/>     |
|  | 14,176    | 9,012     |
|  | <hr/>     | <hr/>     |
| <b>PROPERTY AND EQUIPMENT:</b>   |           |           |
| Land   | 654       | 654       |
| Buildings  | 12,390    | 12,281    |
| Machinery and equipment  | 17,140    | 13,762    |
| Office furniture and equipment   | 15,274    | 13,495    |
| Equipment held for rent  | 4,074     | 3,476     |
| Transportation equipment   | 2,793     | 2,185     |
|  | <hr/>     | <hr/>     |
|  | 52,325    | 45,853    |
| Less accumulated depreciation  | 25,337    | 21,064    |
|  | <hr/>     | <hr/>     |
|  | 26,988    | 24,789    |
|  | <hr/>     | <hr/>     |
|  | \$119,935 | \$102,527 |
|  | <hr/>     | <hr/>     |

See notes to consolidated financial statements

**DAKTRONICS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS (continued)**  
(in thousands, except per share data)

|   | January 31,<br>2004<br>(unaudited) | May 3,<br>2002<br>(audited) |
|---|------------------------------------|-----------------------------|
|   | <hr/>                              | <hr/>                       |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>   |                                    |                             |
| <b>CURRENT LIABILITIES:</b>   |                                    |                             |
| Notes payable, bank   | \$ 91                              | \$ 180                      |
| Accounts payable  | 12,330                             | 9,312                       |
| Accrued expenses  | 11,186                             | 7,790                       |
| Current maturities of long-term debt  | 1,451                              | 2,951                       |
| Billings in excess of costs and estimated earnings  | 7,388                              | 5,528                       |
| Customer deposits   | 2,457                              | 1,709                       |
| Income taxes payable  | 250                                | 1,556                       |
|   | <hr/>                              | <hr/>                       |
| Total current liabilities   | 35,153                             | 29,026                      |
|   | <hr/>                              | <hr/>                       |
| Long-term debt, less current maturities   | 1,669                              | 5,449                       |
| Deferred revenue  | 1,222                              | 1,338                       |
| Deferred income taxes   | 1,760                              | 1,296                       |
|   | <hr/>                              | <hr/>                       |
|   | 4,651                              | 8,083                       |
|   | <hr/>                              | <hr/>                       |
| MINORITY INTEREST IN SUBSIDIARY   | 146                                | 115                         |
|   | <hr/>                              | <hr/>                       |
| <b>SHAREHOLDERS' EQUITY:</b>  |                                    |                             |
| Common stock, no par value, authorized 60,000,000 shares,<br>18,805,675 and 18,596,536 shares issued at January 31, 2004<br>and May 3, 2003, respectively | 15,752                             | 14,654                      |
| Additional paid-in capital  | 746                                | 746                         |
| Retained earnings   | 63,543                             | 49,950                      |
| Treasury stock, at cost, 19,680 shares  | (9)                                | (9)                         |
| Accumulated other comprehensive loss  | (47)                               | (38)                        |
|   | <hr/>                              | <hr/>                       |
|   | 79,985                             | 65,303                      |
|   | <hr/>                              | <hr/>                       |

See notes to consolidated financial statements.

**DAKTRONICS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(in thousands, except per share data)  
(unaudited)

|   | <u>Three Months Ended</u>         |                                   | <u>Nine Months Ended</u>          |                                   |
|---|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|
|   | January 31,<br>2004<br>(13 weeks) | February 1,<br>2003<br>(13 weeks) | January 31,<br>2004<br>(39 weeks) | February 1,<br>2003<br>(40 weeks) |
| Net sales   | \$ 44,745                         | \$ 38,220                         | \$ 151,969                        | \$ 130,400                        |
| Cost of goods sold  | 29,996                            | 25,855                            | 97,914                            | 86,925                            |
| <b>Gross Profit</b>   | <b>14,749</b>                     | <b>12,365</b>                     | <b>54,055</b>                     | <b>43,475</b>                     |
| Operating expenses:   |                                   |                                   |                                   |                                   |
| Selling   | 6,819                             | 5,868                             | 19,695                            | 18,649                            |
| General and administrative                                  | 2,521                             | 1,824                             | 6,858                             | 5,159                             |
| Product design and development                              | 1,893                             | 1,534                             | 6,177                             | 5,086                             |
|   | 11,233                            | 9,226                             | 32,730                            | 28,894                            |
| <b>Operating income</b>                                     | <b>3,516</b>                      | <b>3,139</b>                      | <b>21,325</b>                     | <b>14,581</b>                     |
| Nonoperating income (expense):                              |                                   |                                   |                                   |                                   |
| Interest income   | 258                               | 184                               | 721                               | 516                               |
| Interest expense  | (78)                              | (195)                             | (401)                             | (675)                             |
| Other income, net   | 222                               | 58                                | 571                               | 323                               |
| <b>Income before income taxes<br/>and minority interest</b> | <b>3,918</b>                      | <b>3,186</b>                      | <b>22,216</b>                     | <b>14,745</b>                     |
| Income tax expense  | 1,345                             | 1,288                             | 8,592                             | 5,688                             |
| <b>Income before minority<br/>interest</b>                  | <b>2,573</b>                      | <b>1,898</b>                      | <b>13,624</b>                     | <b>9,057</b>                      |
| Minority interest in (income) of<br>subsidiary              | 43                                | (10)                              | (31)                              | (10)                              |
| <b>Net income</b>   | <b>\$ 2,616</b>                   | <b>\$ 1,888</b>                   | <b>\$ 13,593</b>                  | <b>\$ 9,047</b>                   |
| Earnings per share:   |                                   |                                   |                                   |                                   |
| Basic   | \$ 0.14                           | \$ 0.10                           | \$ 0.73                           | \$ 0.49                           |
| Diluted   | \$ 0.13                           | \$ .10                            | \$ 0.68                           | \$ 0.47                           |

See notes to consolidated financial statements

**DAKTRONICS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**  
(in thousands)  
(unaudited)

|  | <u>Nine Months Ended</u>          |                                   |
|--|-----------------------------------|-----------------------------------|
|  | January 31,<br>2004<br>(39 weeks) | February 1,<br>2003<br>(40 weeks) |
| Cash flows from operating activities:  |                                   |                                   |
| Net income   | \$ 13,593                         | \$ 9,047                          |
| Adjustments to reconcile net income to net cash provided<br>by operating activities: |                                   |                                   |
| Depreciation   | 4,540                             | 4,214                             |
| Amortization   | 100                               | 190                               |
| Minority interest in income of subsidiary  | 31                                | 9                                 |
| Provision for doubtful accounts  | 328                               | (440)                             |
| (Gain) loss on sale of property and equipment  | (304)                             | 743                               |
| Deferred income taxes, net   | 113                               | (592)                             |
| Change in operating assets and liabilities   | (6,301)                           | 943                               |
| <b>Net cash provided by operating activities</b>                                     | <b>12,100</b>                     | <b>14,114</b>                     |

|   |                |                |
|---|----------------|----------------|
| Cash flows from investing activities:                                 |                |                |
| Purchase of property and equipment                                    | (7,100)        | (3,982)        |
| Proceeds from sale of property and equipment                          | 688            | 738            |
|   | <hr/>          | <hr/>          |
| <b>Net cash used in investing activities</b>                          | <b>(6,412)</b> | <b>(3,244)</b> |
|   | <hr/>          | <hr/>          |
| Cash flows from financing activities:                                 |                |                |
| Net payments on notes payable   | (105)          | (51)           |
| Borrowings on long-term debt  | 185            | 1,588          |
| Principal payments on long-term debt                                  | (5,495)        | (6,095)        |
| Proceeds from exercise of stock options and warrants                  | 463            | 441            |
|   | <hr/>          | <hr/>          |
| <b>Net cash used in financing activities</b>                          | <b>(4,952)</b> | <b>(4,117)</b> |
|   | <hr/>          | <hr/>          |
| Effect of exchange rate changes on cash                               | 14             | 13             |
|   | <hr/>          | <hr/>          |
| <b>Increase in cash and cash equivalents</b>                          | <b>750</b>     | <b>6,766</b>   |
|   | <hr/>          | <hr/>          |
| Cash and cash equivalents:  |                |                |
| Beginning   | 9,277          | 2,097          |
|   | <hr/>          | <hr/>          |
| Ending  | \$ 10,027      | \$ 8,863       |
|   | <hr/>          | <hr/>          |
| Supplemental disclosures of cash flow information:                    |                |                |
| Cash payments for:  |                |                |
| Interest  | \$ 403         | \$ 691         |
| Income taxes, net of refunds  | 9,599          | 5,525          |
|   | <hr/>          | <hr/>          |
| Supplemental schedule of non-cash investing and financing activities: |                |                |
| Tax benefits related to exercise of stock options                     | \$ -           | \$ 144         |
|   | <hr/>          | <hr/>          |
| See notes to consolidated financial statements                        |                |                |

**DAKTRONICS, INC. AND SUBSIDIARIES**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

**Note 1. Basis of Presentation**

In the opinion of management, the accompanying unaudited financial statements contain all adjustments necessary to fairly present the Company's financial position, results of operations and cash flows for the periods presented. 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 reported amounts therein. Due to the inherent uncertainty involved in making estimates, actual results in future periods may differ from those estimates.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. The balance sheet at May 3, 2003, has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. These financial statements should be read in conjunction with the Company's financial statements and notes thereto for the year ended May 3, 2003, which are contained in the Company's Annual Report on Form 10-K, previously filed with the Securities and Exchange Commission. The results of operations for the interim periods presented are not necessarily indicative of results that may be expected for any other interim period or for the full fiscal year.

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Star Circuits, Inc., SportsLink, Ltd., Daktronics GmbH, and MSC Technologies, Inc. and its majority-owned subsidiary, Daktronics Canada, Inc. Investments in affiliates owned 50% or less are accounted for by the equity method. Intercompany balances and transactions have been eliminated in consolidation.

**Note 2. Significant Accounting Policies**

**Stock based compensation.** At May 3, 2003, the Company had four stock-based employee compensation plans, which are described more fully in the Company's Annual Report of Form 10-K. The Company accounts for these plans under the recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of FASB Statement No. 123, *Accounting for Stock-Based Compensation*, to stock-based compensation.

|   | <u>Three Months Ended</u> |                     | <u>Nine Months Ended</u> |                     |
|---|---------------------------|---------------------|--------------------------|---------------------|
|   | January 31,<br>2004       | February 1,<br>2003 | January 31,<br>2004      | February 1,<br>2003 |
|   | <hr/>                     | <hr/>               | <hr/>                    | <hr/>               |
| <b>Net Income as reported</b>                                     | \$ 2,616                  | \$ 1,888            | \$ 13,593                | \$ 9,047            |
| Deduct: Total stock-based method<br>employee compensation expense |                           |                     |                          |                     |

determined under fair value based method for all awards, net of related tax effects

|                             |         |         |         |         |
|-----------------------------|---------|---------|---------|---------|
|                             | (110)   | (86)    | (321)   | (263)   |
| <b>Pro forma net income</b> | 2,506   | 1,802   | 13,272  | 8,784   |
| <b>Earnings per share:</b>  |         |         |         |         |
| Basic - as reported         | \$ 0.14 | \$ 0.10 | \$ 0.73 | \$ 0.49 |
| Basic - pro forma           | 0.13    | 0.09    | 0.71    | 0.48    |
| Diluted - as reported       | 0.13    | 0.10    | 0.68    | 0.47    |
| Diluted - pro forma         | 0.13    | 0.09    | 0.67    | 0.45    |

**Commitments and Contingencies.** In connection with certain sales of equipment by the Company, it has agreed to accept a specified level of recourse on the money owed by its customers to other financial institutions. At January 31, 2004 and May 3, 2003, the Company was contingently liable on such recourse agreements in the amounts of \$250, respectively.

The Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, based upon consultation with legal counsel, the ultimate disposition of these matters will not have a material adverse effect on the Company's consolidated financial position.

**Product Warranties.** The Company offers a standard parts coverage warranty for periods varying from one to five years for all of its products. The Company also offers additional types of warranties that include on-site labor, routine maintenance, and event support. In addition, the length of warranty on some installations can vary from one to ten years. The specific terms and conditions of these warranties vary depending on the product sold and customer requirements. The Company estimates the costs that may be incurred under the warranty and records a liability in the amount of such costs at the time product order is received. Factors that affect the Company's warranty liability include historical and anticipated claims cost. The Company periodically assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary.

Changes in the Company's product warranties for the nine months ended January 31, 2004 consisted of the following:

|   |          |
|---|----------|
| Beginning balance - May 4, 2003   | \$ 3,184 |
| Warranties provided for during the period   | 1,566    |
| Settlements made during the period  | (217)    |
| Changes in liability for pre-existing warranties during the period, including expirations | (740)    |
| Ending balance - January 31, 2004   | \$ 3,793 |

**Lease Commitments.** The Company leases office space for various sales and service locations across the country and various equipment, primarily office equipment. Rental expense for operating leases amounted to \$891 and \$678 for the nine months ended January 31, 2004 and February 1, 2003, respectively. Future minimum payments under noncancelable operating leases, excluding executory costs such as management and maintenance fees with initial or remaining terms of one year or more, consisted of the following at January 31, 2004:

|                |                    |          |
|----------------|--------------------|----------|
|                | <u>Fiscal Year</u> |          |
| Remaining for: | 2004               | \$ 175   |
|                | 2005               | 554      |
|                | 2006               | 461      |
|                | 2007               | 284      |
|                | 2008               | 49       |
|                | Total              | \$ 1,523 |

**Purchase Commitments.** From time to time, the Company commits to purchase inventory and advertising rights over periods that extend over a year. It is committed to these purchases through June 2005. As of January 31, 2004, Daktronics, Inc. is obligated to purchase \$4.3 million of inventory and advertising rights through fiscal year 2006 as follows:

|                |                    |          |
|----------------|--------------------|----------|
|                | <u>Fiscal Year</u> |          |
| Remaining for: | 2004               | \$ 642   |
|                | 2005               | 3,515    |
|                | 2006               | 176      |
|                | Total              | \$ 4,333 |

### Note 3. Recently Issued Accounting Pronouncements

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities." This interpretation addresses the requirements for business enterprises to consolidate related entities in which they are determined to be the primary beneficiary as a result of their variable economic interest. The interpretation is intended to provide guidance in judging multiple economic interests in an entity and in determining the primary beneficiary. The interpretation outlines disclosure requirements for variable interest entities in existence prior to January 31, 2003, and outlines consolidation requirements for variable interest entities created after January 31, 2003. This interpretation did not have a material impact on the Company's consolidated financial position or results of operations.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity." SFAS No. 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. SFAS No. 150

is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of SFAS No. 150 did not have a material impact on the Company's consolidated financial position or results of operations.

#### Note 4. Revenue Recognition

*Long-term contracts:* Earnings on long-term contracts are recognized on the percentage-of-completion method, measured by the percentage of costs incurred to date to estimated total costs for each contract. Operating expenses are charged to operations as incurred and are not allocated to contract costs. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are estimable.

*Equipment other than long-term contracts:* The Company recognizes revenue on equipment sales, other than long-term contracts, when title passes, which is usually upon shipment.

*Advertising rights:* The Company occasionally sells and installs its products at facilities in exchange for the rights to sell and retain certain future advertising revenues or payments. It recognizes revenue for the amount of the present value of the future advertising payments or other payments at such time that the payments become fixed and determinable.

On those transactions where the Company has not sold sufficient advertising, that on a present value basis, does not exceed the cost of the equipment, it recognizes revenue and cost of sales to the extent of the advertising sold that is fixed and determinable. Any remaining costs of the equipment are capitalized as advertising rights and recognized as additional advertising contracts are sold. It also regularly reviews these rights for any impairment.

Advance collections of advertising revenues are recorded as deferred income. The cost of advertising rights, net of amortization, was \$636 as of January 31, 2004 and \$385 as of May 3, 2003.

*Product maintenance:* In connections with the sale of the Company's products, it also occasionally sells separately priced extended warranties and product maintenance contracts. The revenue related to such contracts are deferred and recognized as net sales over the term of the contracts, which varies from one to ten years.

*Software:* The Company typically sells its proprietary software bundled with its displays and certain other products. Pursuant to American Institute of Certified Public Accountants ("AICPA") Statement of Position ("SOP") 97-2, "Software Revenue Recognition," as amended by SOP 98-4, "Deferral of the Effective Date of a Provision of SOP 97-2" and SOP 98-9, "Modification of SOP 97-2, Software Revenue Recognition with Respect to Certain Transactions," revenues from software license fees on sales, other than long-term contracts, are recognized when persuasive evidence of an agreement exists, delivery of the product has occurred, the fee is fixed or determinable and collection is probable. For sales of software, included in long-term contracts, the revenue is recognized under the percentage-of-completion method for long-term contracts starting when the above-mentioned criteria have been met.

*Services:* Revenues generated by the Company for services such as event support, control room design, on-site training, equipment service and continuing technical support for operators of the Company's equipment are recognized as net sales as the services are performed.

#### Note 5. Earnings Per Share

Basic EPS is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that would occur if securities or other obligations to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Company.

A reconciliation of the income and common share amounts used in the calculation of basic and diluted earnings per share (EPS) for the three and nine months ended January 31, 2004 and February 1, 2003 follows:

|  | Net Income | Shares     | Per Share Amount |
|--|------------|------------|------------------|
| For the three months ended January 31, 2004: |            |            |                  |
| Basic earnings per share                     | \$ 2,616   | 18,750,366 | \$ 0.14          |
| Effect of dilutive securities:               |            |            |                  |
| Exercise of stock options and warrants       | -          | 1,261,890  | (0.01)           |
| Diluted earnings per share                   | \$ 2,616   | 20,012,256 | \$ 0.13          |
| For the three months ended February 1, 2003: |            |            |                  |
| Basic earnings per share                     | \$ 1,888   | 18,382,970 | \$ 0.10          |
| Effect of dilutive securities:               |            |            |                  |
| Exercise of stock options and warrants       | -          | 1,313,903  | -                |
| Diluted earnings per share                   | \$ 1,888   | 19,696,873 | \$ 0.10          |
| For the nine months ended January 31, 2004:  |            |            |                  |
| Basic earnings per share                     | \$ 13,593  | 18,655,109 | \$ 0.73          |
| Effect of dilutive securities:               |            |            |                  |
| Exercise of stock options and warrants       | -          | 1,210,622  | (0.05)           |
| Diluted earnings per share                   | \$ 13,593  | 19,865,731 | \$ 0.68          |
| For the nine months ended February 1, 2003:  |            |            |                  |
| Basic earnings per share                     | \$ 9,047   | 18,329,934 | \$ 0.49          |
| Effect of dilutive securities:               |            |            |                  |
| Exercise of stock options and warrants       | -          | 1,066,409  | (0.02)           |

|                            |    |       |            |    |      |
|----------------------------|----|-------|------------|----|------|
| Diluted earnings per share | \$ | 9,047 | 19,396,343 | \$ | 0.47 |
|----------------------------|----|-------|------------|----|------|

## Note 6. Goodwill and Other Intangible Assets — Adoption of SFAS No. 142

Effective April 28, 2002, the Company adopted SFAS No. 142 "Goodwill and Other Intangible Assets." This statement prohibits the amortization of goodwill and intangible assets with indefinite useful lives and requires that these assets be reviewed for impairment at least annually. An impairment charge is recognized only when the calculated fair value of a reporting unit, including goodwill, is less than its carrying amount. The Company performed an analysis as of October 25, 2002. The results of the analysis indicated that no goodwill impairment existed as of October 25, 2002. In accordance with the SFAS 142, the Company will complete an impairment analysis on an annual basis.

Goodwill, net of accumulated amortization, was \$1,083 at January 31, 2004 and \$1,043 at May 3, 2003. Accumulated amortization was \$157 at January 31, 2004 and at May 3, 2003.

As required by SFAS No. 142, intangibles with finite lives continue to be amortized. Included in intangible assets are a non-compete agreement and a patent license. Intangible assets before accumulated amortization were \$550 at January 31, 2004 and May 3, 2003. Accumulated amortization was \$473 and \$419 at January 31, 2004 and May 3, 2003, respectively. The net value of intangible assets is included as a component of intangible and other assets in the accompanying consolidated balance sheets. Estimated amortization expense based on intangibles as of May 3, 2003, is \$63, \$40, and \$27 for the fiscal years ending 2004, 2005, and 2006, respectively.

## Note 7. Inventories

Inventories consist of the following:

|                  | January 31 2004  |           | May 3, 2003   |
|------------------|------------------|-----------|---------------|
| Raw Materials    | \$ 7,508         | \$        | 5,999         |
| Work-in-progress | 2,918            |           | 2,151         |
| Finished goods   | 7,578            |           | 6,713         |
|                  | <u>\$ 18,004</u> | <u>\$</u> | <u>14,863</u> |

## Note 8. Segment Disclosure

The Company's chief operating decision maker reviews financial information presented on a consolidated basis, accompanied by disaggregated information about revenue and certain expenses, by market and geographic region, for purposes of assessing financial performance and making operating decisions. Accordingly, the Company considers itself to be operating in a single industry segment. The Company does not manage its business by solution or focus area. During the quarter the Company recognized approximately \$5.1 million in net sales relating to the previously announced transaction with the Cleveland Indians.

The Company does not maintain information on sales by products, and therefore, disclosure of such information is not practical.

The following table presents information about the Company by geographic area:

|                                      | United States |    | Other  |    | Total   |
|--------------------------------------|---------------|----|--------|----|---------|
| Net sales for the nine months ended: |               |    |        |    |         |
| January 31, 2004                     | \$ 130,881    | \$ | 21,088 | \$ | 151,969 |
| February 1, 2003                     | 124,925       |    | 5,475  |    | 130,400 |
| Long-lived assets at:                |               |    |        |    |         |
| January 31, 2004                     | 28,690        |    | 883    |    | 29,573  |
| February 1, 2003                     | 26,782        |    | 308    |    | 27,090  |

## Note 9. Subsequent Event

In February 2004 the Company entered into a letter of intent to acquire the minority interest in Daktronics Canada, Inc., an 80% owned subsidiary, for approximately \$460 to be paid through issuance of stock in Daktronics, Inc. The acquisition is expected to close prior to March 15, 2004. The acquisition of this minority interest is contingent on negotiation of the final purchase agreement and is not expected to have a material effect on operations.

## Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion highlights the principal factors affecting changes in financial condition and results of operations. This discussion should be read in conjunction with the accompanying Consolidated Financial Statements and Notes to Consolidated Financial Statements.

### OVERVIEW

The Company designs, manufactures, and sells a wide range of computer-programmable information display systems to customers in a variety of markets throughout the world. The Company focuses its sales and marketing efforts on geographical regions, markets and products. The primary categories of markets include sport, commercial, and transportation.

The Company's net sales and profitability historically have fluctuated due to the impact of large product orders, such as display systems for major league sport facilities and colleges and universities, as well as seasonality factors, including the timing of the various sports seasons and the impact of holidays, which primarily impact the Company's third quarter. The Company's gross margins on large product orders tend to fluctuate more than those for small standard orders. Large product orders that involve competitive bidding and substantial subcontract work for product installation generally have lower gross margins. Although the Company follows the percentage of completion method of recognizing revenues for larger custom orders, the Company nevertheless has experienced fluctuations in operating results and expects that its future results of operations may be subject to similar fluctuations.

The Company books orders only upon receipt of a firm contract and, in most cases, only after receipt of any required deposits related to the order. As a result, certain orders for which the Company has received binding letters of intent or contracts will not be booked until all required contractual documents and deposits are received. In addition, order bookings can vary significantly as a result of the timing of large orders.

The Company operates on a 52-53 week fiscal year, with fiscal years ending on the Saturday closest to April 30 of each year. Fiscal year 2003 contained 53 weeks and the first nine months of fiscal year 2003 contained 40 weeks as compared to the more typical 52-week year and 39-week nine month period. Fiscal year 2004 contains 52 weeks.

For a summary of recently issued accounting pronouncements and the effects of those pronouncements on the financial results of the Company, refer to Note 3 of the consolidated financial statements of the Company, which are included elsewhere in this report.

## CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The following discussion and analysis of financial condition and results of operations are based upon the Company's Consolidated Financial Statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On a regular basis, the Company evaluates its estimates, including those related to estimated total costs on long-term contracts, estimated costs to be incurred for product warranties and extended maintenance contracts, bad debts, excess and obsolete inventory and contingencies. Its estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The Company believes the following critical accounting policies require significant judgments and estimates in the preparation of its consolidated financial statements:

*Revenue recognition on long-term contracts.* Earnings on long-term contracts are recognized on the percentage-of-completion method, measured by the percentage of costs incurred to date to estimated total costs for each contract. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are estimatable. Generally, contracts entered into by the Company have fixed prices established and to the extent the actual costs to complete contracts are higher than the amounts estimated as of the date of the financial statements, the resulting gross margin would be negatively effected in future quarters when the Company revises its estimates. The Company's practice is to revise estimates as soon as such changes in estimates are known.

*Allowance for doubtful accounts.* The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. If the financial condition of its customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. As of January 31, 2004, the Company had an allowance for doubtful accounts balance of approximately \$1.2 million.

*Warranties.* The Company has created a reserve for warranties on its products equal to its estimate of the actual costs to be incurred in connection with its performance under the standard warranty. In the event that the Company would become aware of an increase in its warranty reserves additional reserves may become necessary, resulting in an increase in costs of goods sold. As of January 31, 2004, the Company had a total of approximately \$3.8 million deferred for these costs.

*Extended warranty and product maintenance.* The Company has deferred revenue related to separately priced extended warranty and product maintenance agreements. In the event that the Company would become aware of an increase in its estimated costs under these agreements in excess of its deferred revenue, additional reserves may be necessary, resulting in an increase in costs of goods sold. During the first nine months of fiscal year 2004, approximately \$1.6 million in additional reserves were provided for.

*Inventory.* Inventories are stated at the lower of cost or market. Market refers to the current replacement cost, except that market may not exceed the net realizable value (i.e., estimated selling price in the ordinary course of business less reasonable predictable costs of completion and disposal); and market is not less than the net realizable value reduced by an allowance for normal profit margins. In valuing inventory the Company estimates market value where it is believed to be the lower of cost or market and any necessary charges are charged to costs of goods sold in the period in which it occurs. All other inventory is valued at cost.

## RESULTS OF OPERATIONS

The following table sets forth the percentage of net sales represented by items included in the Company's Consolidated Statements of Operations for the periods indicated:

|                    | <b>Three Months Ended</b>                  |  | <b>Nine Months Ended</b>                   |  |
|--------------------|--|--|--|--|
|                    | <b>January 31,<br/>2004<br/>(13 weeks)</b> | <b>February 1,<br/>2003<br/>(13 weeks)</b> | <b>January 31,<br/>2004<br/>(39 weeks)</b> | <b>February 1,<br/>2003<br/>(40 weeks)</b> |
| Net sales          | 100.0%                                     | 100.0%                                     | 100.0%                                     | 100.0%                                     |
| Cost of goods sold | 67.0%                                      | 67.7%                                      | 64.4%                                      | 66.7%                                      |
| Gross profit       | 33.0%                                      | 32.3%                                      | 35.6%                                      | 33.3%                                      |
| Operating expense  | 25.1%                                      | 24.1%                                      | 21.6%                                      | 22.1%                                      |
| Operating income   | 7.9%                                       | 8.2%                                       | 14.0%                                      | 11.2%                                      |

|  |        |        |        |        |
|--|--------|--------|--------|--------|
| Interest income                                  | 0.5%   | 0.5%   | 0.5%   | 0.4%   |
| Interest expense                                 | (0.2%) | (0.5%) | (0.3%) | (0.5%) |
| Other income, net                                | 0.5%   | 0.1%   | 0.4%   | 0.2%   |
|  | <hr/>  | <hr/>  | <hr/>  | <hr/>  |
| Income before income taxes and minority interest | 8.7%   | 8.3%   | 14.6%  | 11.3%  |
| Income tax expense                               | 3.0%   | 3.4%   | 5.7%   | 4.4%   |
| Minority interest in (income) loss of subsidiary | 0.1%   | (0.0%) | (0.0%) | (0.0%) |
|  | <hr/>  | <hr/>  | <hr/>  | <hr/>  |
| Net income                                       | 5.8%   | 4.9%   | 8.9%   | 6.9%   |
|  | <hr/>  | <hr/>  | <hr/>  | <hr/>  |

## NET SALES

Net sales increased 17.1% to \$44.7 million for the quarter ended January 31, 2004, as compared to \$38.2 million for the same period in fiscal year 2003. Net sales increased 16.5% to \$152.0 million for the nine months ended January 31, 2004, as compared to \$130.4 million for the same period in fiscal year 2003. For the quarter ended January 31, 2004, net sales increased in the sports and commercial market, but were down in the transportation market. Net sales were also up in the United States and internationally both for the quarter and for the nine months of the year. Finally, as a percent of overall net sales, standard product orders were more than 34% of net sales for the third quarter of fiscal year 2004 as compared to approximately 23% for the third quarter of fiscal year 2003. Year to date standard product orders were in excess of 28% of total net sales as compared to 25% for the first nine months of fiscal year 2003.

Within the sports markets, the growth in the third quarter of fiscal year 2004 as compared to the third quarter of fiscal year 2003 was mainly in sales to high schools and smaller sports facilities and major league sports facilities. Sales to mid-sized institutions, including colleges and universities, were relatively flat for the quarter. Year to date sales were up across all three areas, led primarily by growth in major league sports facilities followed by growth in net sales to high schools and smaller facilities. During the first three quarters of the year, the Company completed a number of large installations that contributed to the growth both in the quarter and year to date as compared to the same periods of the last fiscal year. The Company expects that sales will be up for the year in the smaller sports facilities and in the larger professional facilities, while the college and university market will be up only slightly over the previous year. During the quarter net sales included approximately \$5.1 million or 13.1% of net sales related to the contract the company had previously announced with the Cleveland Indians. The growth in the high school portion of the sports market is partially attributable to the growth in sales of video displays, primarily for football stadiums and other factors as listed below. The growth in the sports market as a whole was due to a number of factors, including the overall level of order bookings during the quarter and the growth in opportunities outside the United States. In addition, the Company benefits from its network of sales and service offices throughout the country, giving it the ability to serve its customers more effectively. The Company believes that the effects of the slow economy have a lesser impact on the sports market, as compared to its other markets, since its products are generally revenue generation tools (through advertising) for facilities and the sports business in general is a more resistant to negative factors in the economy as a whole.

Orders in the sports market were up in the third quarter of fiscal year 2004 as compared to the third quarter of fiscal year 2003, primarily due to the factors listed above and due to the booking of two large orders with major league baseball teams. Order bookings were also up in the smaller sports facilities and internationally. During the quarter, the Company continued to benefit from growth opportunities presented through its sports marketing business as it signed additional orders, which included sponsorships by advertisers. This has helped drive sales in smaller facilities as well as mid-sized facilities. The Company believes that the growth in the sports market continues to be driven by growth internationally, new product development, an expanding market as the Company's products have become more affordable to more institutions, and its overall product offerings, which the Company believes are the most complete and integrated systems in the marketplace.

Net sales in the commercial market grew significantly during the third quarter of fiscal year 2004 as compared to the same period of fiscal year 2003. Sales of standard products were especially strong primarily due to growth in sales to national accounts and the continued acceptance of the Company's Galaxy® display product line. On a year to date basis, this portion of the Company's business has experienced the greatest percentage growth as compared to the other two markets again due to a large degree to sales outside the United States and the national account business. Order bookings were also up by almost 70% for the third quarter of fiscal year 2004 and for the first three quarters of the year as compared to the same periods of fiscal year 2003. Although sales and orders in the commercial market are dependant to a large degree on current economic conditions, the Company has been able to grow the business due to its product offerings, its international expansion, the network of sales and service offices throughout the country, the development of resellers, primarily in the United States, and the integrated offerings the Company provides. As the Company continues to penetrate the opportunities in the commercial market, including national accounts and business outside of the United States, and further matures its regional sales force, it expects the trend of increasing standard order volume to continue double-digit percentage growth rates. The Company's ability to generate greater sales to national accounts and other large customers, domestically and internationally, could cause this rate of growth to develop at a faster rate.

Net sales in the transportation markets decreased during the third quarter of fiscal year 2004 as compared to the same period of fiscal 2003 primarily due to the decline in order bookings that the Company experienced in the first and second quarter of the current fiscal year. For the first nine months of fiscal year 2004, net sales in the transportation market were relatively flat as compared to fiscal year 2003. The decline for the quarter and year to date has been in the Intelligent Transportation Systems portion of the market as opposed to the aviation portion of the market, which is up for both the quarter and year to date. Year to date, both portions of the transportation market were down in terms of order bookings however the Company expects that for the year the transportation market will increase year over year in orders while sales may be relatively flat.

The Company occasionally sells products in exchange for the proceeds of advertising revenues generated from use of products. These sales represented less than 10% of net sales for the third quarter and nine months ended January 31, 2004. The gross profit on these net sales has typically been higher than the gross profit margin on other net sales of similar size, although the selling expenses associated with these transactions are typically higher.

The order backlog as of January 31, 2004 was approximately \$43 million as compared to \$51 million as of February 1, 2003, and \$39 million at the beginning of the third quarter of fiscal year 2004. Historically, the Company's backlog varies significantly due to the timing of large orders. The decrease in backlog for the third quarter of fiscal year 2003 was primarily concentrated in the sports markets and transportation markets, while the commercial market backlog experienced significant growth on a percentage basis from the end of the third quarter of fiscal year 2003. As compared to the beginning of the third quarter of fiscal year 2004, the backlog increased in all the markets, however the actual dollar increase was the most significant in the sports market.

## GROSS PROFIT

Gross profit increased 19.3% to \$14.7 million as compared to \$12.4 million for the third quarter of fiscal year 2003. Gross profit increased 24.3% to \$54.1 million for the nine months ended January 31, 2004, compared to \$43.5 million for the same period in fiscal year 2003. As a percent of net sales, gross profit was

33.0% and 35.6% for the three and nine months ended January 31, 2004, as compared to 32.3% and 35.6% for the three and nine months ended February 1, 2003. The increase in gross profit for both the three and nine months was due to a number of factors including lower raw material costs, the benefits of signing orders in advance of raw material price declines, improvements in on-site project costs as compared to estimates (primarily in the first half of fiscal year 2004), an improvement in expected margins at contract signing, improved overhead absorption in manufacturing (primarily in the third quarter of fiscal year 2004) and an improved mix between higher margin standard products and large contracts. These improvements were offset by increased freight costs, inventory losses, and for the third quarter, an accrual for anticipated profit sharing plan contributions. The Company continues to strive towards higher gross margins, as a percent of net sales, although depending on the actual mix and level of future sales, margin percentages may not increase and are likely to decrease from the levels of the first three quarters as a whole. The Company expects that margins will be similar for the fourth quarter of fiscal year 2004 as compared to the fourth quarter of fiscal year 2003, although as a result of various factors, the actual amount could vary significantly.

## OPERATING EXPENSES

*Operating expenses.* Operating expenses, which are comprised of selling, general and administrative, and product design and development costs, increased by approximately 21.8% from \$9.2 million in the third quarter of fiscal year 2003 to \$11.2 million in the third quarter of fiscal year 2004. As a percent of net sales, operating expenses increased from 24.1% to 25.1%. For the nine months ended January 31, 2004, operating expenses increased 13.3% from \$28.9 million to \$32.7 million. For the nine months ended February 1, 2003, all components of operating expenses were affected as a result of the first quarter of fiscal year 2003 containing 14 weeks as opposed to the 13 weeks included in the first quarter of fiscal year 2004. In addition, during the third quarter, the Company accrued amounts for anticipated profit sharing plan contributions, not previously accrued, that affected all areas.

*Selling Expenses.* Selling expenses consist primarily of salaries, other employee related costs, travel and entertainment, facilities-related costs for sales and service offices, and expenditures for marketing efforts including such things as collateral materials, conventions and trade shows, product demos and supplies.

Selling expenses increased 16.2% to \$6.8 million for the three months ended January 31, 2004, as compared to \$5.9 million for the same period in fiscal year 2003. Selling expenses increased 5.6% to \$19.7 million for the nine months ended January 31, 2004 from \$18.6 million for the same period in fiscal year 2003. Selling expenses decreased to 15.2% of net sales for the third quarter of fiscal year 2004 from 15.4% of net sales for the third quarter of fiscal year 2003. For the nine months ended January 31, 2004, selling expenses were 13.0% of net sales as compared to 14.3% of net sales for the nine months ended February 1, 2003.

Selling expenses for the quarter were higher as a result of an increase in personnel costs as the Company continued to build its sales infrastructure in line with the growth in net sales, higher travel and entertainment costs due to the increased level of net sales, and costs associated with the growth in the number of sales and service offices. The increase in selling expenses for the first nine months of fiscal year 2004 as compared to the first nine months of fiscal year 2003 was the result of higher personnel costs and related infrastructure costs of its sales and service office network, higher travel and entertainment costs due to the increased level of net sales, offset by lower product demo costs and lower bad debt expense. The Company expects selling expense to increase slightly each quarter in the future, although the fourth quarter costs could end up equal or less than the current quarter's costs. As a percentage of net sales, selling expenses are expected to be at or lower than the level achieved for all of fiscal year 2003.

*General and Administrative.* General and administrative expenses consist primarily of salaries, other employee-related costs, professional fees, shareholder relations fees, facilities and equipment related costs for administration departments, amortization of intangibles, and supplies.

General and administrative expenses increased 38.2% to \$2.5 million for the three months ended January 31, 2004 compared to \$1.8 million for the same period in fiscal year 2003. General and administrative expenses increased 32.9% to \$6.9 million for the nine months ended January 31, 2004 as compared to \$5.2 million for the first nine months ended February 1, 2003. General and administrative expenses increased to 5.6% as a percent of net sales for the third quarter of fiscal year 2004 from 4.8% of net sales for the third quarter of fiscal year 2003. For the nine months ended January 31, 2004, general and administrative expenses were 4.5% of net sales as compared to 4.0% of net sales for the nine months ended February 1, 2003.

The increase for the third quarter of fiscal year 2004 as compared to the third quarter of fiscal year 2003 was due to increases in software, information systems consulting costs, the effects of compensation paid under employment agreements associated with a previous acquisition, higher professional fees related primarily to the expansion of the Company's business outside of the United States, costs associated with union attempts to represent certain manufacturing employees, the costs of implementing the requirements of the Sarbanes-Oxley Act and related regulations, and higher training costs related to the increased level of employees company wide. These increases were offset by lower costs of shareholder relations expenses and amortization costs. For the first three quarters of fiscal year 2004 general and administrative costs increased as a result of the factors mentioned above, plus increased costs of personnel in all administrative areas, higher corporate insurance costs as a result of the insurance market as a whole, and higher charitable contribution costs and other employee benefits. These increases were offset by declines in costs of shareholder relations. The Company expects that general and administrative costs will decline in the fourth quarter of fiscal year 2004 followed by increases in following quarters at a rate slower than the rate of growth in net sales.

As mentioned above and as previously mentioned in filings, a union had been seeking to represent certain manufacturing employees. During the quarter, a vote was held that overwhelmingly rejected the union representation. The Company believes that overall relations with employees are good, although as a result of this activity, it is exploring various ways to improve relations further.

*Product Design and Development.* Product design and development expenses consist primarily of salaries, other employee-related costs, facilities and equipment related costs, and supplies.

Product design and development expenses increased 23.4% to \$1.9 million for the nine months ended January 31, 2004 as compared to \$1.5 million for the nine months ended February 1, 2003. Product design and development expenses increased 21.5% to \$6.2 million for the nine months ended January 31, 2004 compared to \$5.1 million for the same period in fiscal year 2003. Product design and development was 4.2% as a percent of net sales for the third quarter of fiscal year 2004 and 4.0% of net sales for the third quarter of fiscal year 2003. For the nine months ended January 31, 2004, product design and development expenses were 4.1% of net sales as compared to 3.9% of net sales for the nine months ended February 1, 2003. Generally, product design and development expenses increase during times when the Company's engineering resources are not dedicated to long-term contracts, as the same personnel who work on research and development also work on long-term contracts. During the quarter the Company invested in a number of critical initiatives including further development of its controllers, various software solutions, video and matrix displays, and product enhancements.

The Company expects that product design and development expenses will approximate 4.0% of net sales on an annual basis.

## INTEREST INCOME

The Company occasionally sells products on an installment basis, under lease arrangements or in exchange for the rights to sell and retain advertising revenues related to the scoreboard, display and facility, which result in long-term receivables. Interest income resulting from these long-term receivables increased 40.2% to \$0.3 million for the quarter ended January 31, 2004, as compared to \$0.2 million for the third quarter of fiscal year 2003. For the nine months ended January 31, 2004, interest income increased 39.7% to \$0.7 million from \$0.5 million for the nine months ended February 1, 2003. The increase for both periods of time was the result of higher average levels of long-term receivables outstanding during the respective periods.

## **INTEREST EXPENSE**

Interest expense is comprised primarily of interest costs on the Company's long-term debt. Interest expense decreased 60.0% to \$0.1 million for the third quarter of fiscal year 2004 as compared to \$0.2 million for the third quarter of fiscal year 2003. For the nine months ended January 31, 2004, interest expense declined 40.6% to \$0.4 million from \$0.7 million for the nine months ended February 1, 2003. The decrease for both the nine months and the quarter was due to the reduction of debt outstanding under the Company's line of credit and decreases in average long-term debt outstanding, which was partially offset by penalties (in the first quarter of fiscal year 2004) the Company paid to retire debt ahead of its scheduled maturity.

## **OTHER INCOME, NET**

Other income, net increased from \$0.1 million to \$0.2 million for the third quarter of fiscal year 2004 as compared to the third quarter of fiscal year 2003. It increased to \$0.6 million for the first nine months of fiscal year 2004 as compared to \$0.3 million in the first nine months of fiscal year 2003. The increase for the nine months was primarily the result of gains realized on the sale of the rental equipment used by the Company's video display rental subsidiary. The increase in the third quarter of fiscal year 2004 as compared to the same quarter of fiscal year 2003 was due to the sale of assets related to the Company's voting system business. The Company will continue supplying displays to this market but has exited the customized software portion of the business and related maintenance obligations.

## **LIQUIDITY AND CAPITAL RESOURCES**

Working capital was \$43.6 million at January 31, 2004, and \$39.7 million at May 3, 2003. The Company has historically financed working capital needs through a combination of cash flow from operations and borrowings under bank credit agreements.

Cash provided by operations for the nine months ended January 31, 2004, was \$12.1 million. Net income of \$13.6 million plus depreciation and amortization of \$4.6 million, an increase in accounts payable and accrued expenses, and billings in excess of costs and profits was offset by an increase in accounts receivable, inventories, estimated earnings in excess of billings, and long term receivables. The changes in operating assets and liabilities were primarily related to the growth of the Company during the first nine months of the year. In addition, as a result of the timing of certain large projects, the Company received larger than normal amounts of inventory during the last week of the quarter, creating an increase in accounts payable and inventory. The growth in long-term receivables resulted from the growth in the sports marketing business of the Company and the financing of contracts on an installment basis.

Cash used by investing activities consisted of \$7.1 million of purchases of property and equipment. During the first nine months of fiscal year 2004, the Company invested approximately \$0.6 million in transportation equipment, \$2.7 million in manufacturing equipment that added significant capacity in the electronic assembly and the metal fabrication areas, \$1.8 million in information systems infrastructure, including software, \$0.9 million in product demonstration equipment, and \$0.9 million in rental equipment, primarily for its Sports Link subsidiary. These investments were made to support the Company's continued growth, to increase capacity, and to replace obsolete equipment.

Cash used by financing activities included a \$5.5 million net reduction of long-term debt arrangements and offset by \$0.5 million in proceeds from the exercise of stock options.

The Company has used and expects to continue to use cash reserves and bank borrowings to meet its short-term working capital requirements. On large product orders, the time between order acceptance and project completion may extend up to and exceed 18 months depending on the amount of custom work and the customer's delivery needs. The Company often receives a down payment or progress payments on these product orders. To the extent that these payments are not sufficient to fund the costs and other expenses associated with these orders, the Company uses working capital and bank borrowings to finance these cash requirements.

The Company's product development activities include the enhancement of existing products and the development of new products from existing technologies. Product design and development expenses were \$1.9 million for the quarter ended January 31, 2004. The Company intends to continue to incur these expenditures to develop new display products using various display technologies to offer higher resolution, and more cost effective and energy efficient displays. The Company also intends to continue developing software applications for its display controllers to enable these products to continue to meet the needs and expectations of the marketplace.

The Company has a credit agreement with a bank that provides for a \$20.0 million line of credit, which includes up to \$2.0 million for standby letters of credit. The interest rate on the line of credit is equal to LIBOR plus 1.55% (1.1% at January 31, 2004) and is due on October 1, 2005. As of January 31, 2004, no advances under the line of credit were outstanding. Two standby letters of credit were issued and outstanding for approximately \$1.1 million as of January 31, 2004. These letters of credit were issued primarily to support the issuance of a bid guarantee on a project. The credit agreement is unsecured and requires the Company to meet certain covenants including the maintenance of tangible net worth of at least \$40 million, a minimum liquidity ratio, a limit on dividends and distributions, and a minimum adjusted fixed charge coverage ratio. Daktronics Canada, Inc., the Company's Canadian subsidiary, has various credit agreements that provide up to \$0.3 million in borrowings under lines of credit. The interest rate on the lines of credit is equal to 1% above the prime rate of interest (4.25% at January 31, 2004). As of January 31, 2004, \$0.1 had been drawn under the line. The lines are secured primarily by accounts receivables, inventory and other assets of the subsidiary.

The Company is sometimes required to obtain performance bonds for display installations and currently has a bonding line available through a surety company that provides for an aggregate of \$100.0 million in bonded work outstanding. At January 31, 2004, the Company had approximately \$7.1 million of bonded work outstanding against this line.

The Company believes under its current growth estimates over the next year, it has sufficient capacity under its line of credit. Beyond that time, it may need to increase the amount of its credit facility depending on various factors. The Company anticipates that it will be able to obtain any needed funds under commercially reasonable terms from its current lender. The Company believes that cash from operations, from its existing or increased credit facility, and its current working capital will be adequate to meet the cash requirements of its operations in the foreseeable future.

### Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

#### FOREIGN CURRENCY EXCHANGE RATES

Through January 31, 2004, substantially all of the Company's net sales were denominated in United States dollars, and its exposure to foreign currency exchange rate changes has not been significant. Net sales originating outside the United States for the third quarter of fiscal year 2004 were 13.9% of total net sales. The Company operates in Canada through a majority owned subsidiary. Sales of the Canadian subsidiary comprised 3.8% of net sales in the first half of fiscal year 2004. In the event the Company believed that currency risk in Canada was significant it would utilize foreign exchange hedging contracts to manage its exposure to the Canadian dollar.

During the first half of fiscal year 2004, the Company entered into an order denominated in euros. To minimize its risk on fluctuations in euros versus the United States dollar, it entered into a forward contract to sell euros, net of its euro denominated obligations on the contract.

It is expected that in the future net sales denominated in foreign currency may increase as a percentage of net sales. As a result, operating results may become subject to fluctuations based upon changes in the exchange rates of certain currencies in relation to the United States dollar. To the extent that the Company engages in international sales denominated in United States dollars, an increase in the value of the United States dollar relative to foreign currencies could make the Company's products less competitive in international markets. Although the Company will continue to monitor and minimize its exposure to currency fluctuations, and, when appropriate, may use financial hedging techniques in the future to minimize the effect of these fluctuations, exchange rate fluctuations as well as differing economic conditions, changes in political climates, differing tax structures and other rules and regulations could adversely affect the Company's financial results in the future.

#### INTEREST RATE RISKS

The Company's exposure to market rate risk for changes in interest rates relates primarily to the Company's debt and long-term accounts receivable. The Company maintains a blend of both fixed and floating rate debt instruments. As of January 31, 2004, the Company's outstanding debt approximated \$3.1 million, substantially all of which was in fixed rate obligations. Each 100 basis point increase or decrease in interest rates would have an insignificant annual effect on variable rate debt interest based on the balances of such debt as of January 31, 2004. For fixed rate debt, interest rate changes affect its fair market value, but do not impact earnings or cash flows.

In connection with the sale of certain video displays, scoreboards, and message displays, the Company has entered into various types of financings. The aggregate amounts due from customers include an imputed interest element. The majority of these financings carry fixed rates of interest. As of January 31, 2004, the Company's outstanding long-term receivables were approximately \$15.3 million. Each 25 basis point increase in interest rates would have an associated annual opportunity cost of approximately \$0.1 million.

The following table provides information about the Company's financial instruments that are sensitive to changes in interest rates, including debt obligations for the quarter ending May 1, 2004, and fiscal years following fiscal year 2004.

|  | Principal (Notional) Amount by Expected Maturity |       |       |       |       |                 |
|--|--|-------|-------|-------|-------|-----------------|
|  | (dollars in thousands)                           |       |       |       |       |                 |
|  | Fiscal Year Ending                               |       |       |       |       |                 |
|  | 2004   | 2005  | 2006  | 2007  | 2008  | There-<br>after |
| <b>Assets:</b>                                       |  |       |       |       |       |                 |
| Long-term receivables,<br>including current portion: |  |       |       |       |       |                 |
| Fixed rate   | 1,658  | 2,689 | 3,631 | 1,796 | 1,657 | 3,869           |
| Average interest rate                                | 5.8%   | 8.1%  | 8.9%  | 7.5%  | 7.5%  | 6.9%            |
| <b>Liabilities:</b>                                  |  |       |       |       |       |                 |
| Long and short term debt                             |  |       |       |       |       |                 |
| Fixed rate   | 469  | 1,400 | 1,117 | 144   | 45    | 36              |
| Average interest rate                                | 6.1%   | 8.2%  | 8.2%  | 8.3%  | 9.1%  | 11.4%           |

The carrying amounts reported on the balance sheet for long-term receivables and long and short-term debt approximates its fair value.

Substantially all of the Company's cash balances are denominated in United States dollars. Cash balances in foreign currencies are operating balances maintained in accounts of the Company's Canadian subsidiary and an account of the Company to settle euro-based payments. These balances are immaterial to the Company as a whole.

### Item 4. CONTROLS AND PROCEDURES

Based on an evaluation of the Company's disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q, James B. Morgan, President and Chief Executive Officer of the Company, and William R. Retterath, Chief Financial Officer and Treasurer of the Company, have concluded that the Company's disclosure controls and procedures are effective in ensuring that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission's rules and forms. There were no significant changes in the Company's internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

## PART II. OTHER INFORMATION

### Item 1. LEGAL PROCEEDINGS

*Not Applicable*

**Item 2. CHANGES IN SECURITIES AND USE OF PROCEEDS**

*Not Applicable*

**Item 3. DEFAULTS UPON SENIOR SECURITIES**

*Not Applicable*

**Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

*Not Applicable*

**Item 5. OTHER INFORMATION**

*Not Applicable*

**Item 6. EXHIBITS AND REPORTS ON FORM 8-K**

(a) Exhibits

- Ex. 10.14 FOURTH AMENDMENT, DATED DECEMBER 2, 2003 TO THE LOAN AGREEMENT DATED OCTOBER 14, 1998 BETWEEN US BANK NATIONAL ASSOCIATION AND DAKTRONICS, INC.
- Ex. 31.1 CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER REQUIRED BY RULE 13a-14(a) OR RULE 15d-14 (a) OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002
- Ex. 31.2 CERTIFICATION OF THE CHIEF FINANCIAL OFFICER REQUIRED BY RULE 13a-14(a) OR RULE 15d-14 (a) OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002
- Ex. 32.1 CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002
- Ex. 32.2 CERTIFICATION OF THE CHIEF FINANCIAL OFFICER PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

(b) Reports on Form 8-K

The following current reports on Form 8-K were filed by the Company during the third fiscal quarter:

Current report on Form 8-K dated November 19, 2003 setting forth the earning release for the second quarter of fiscal year 2004.

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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. After due inquiry and to the best of my knowledge and belief, I certify that the information set forth in this statement is true, complete and correct.

By: /s/ William R. Retterath  
Daktronics, Inc.  
William R. Retterath,  
Chief Financial Officer and Treasurer  
Principal Financial Officer

Date: February 20, 2004

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## FOURTH AMENDMENT TO LOAN AGREEMENT AND REVOLVING NOTE

This Fourth Amendment to Loan Agreement and Revolving Note is made and entered into this 2nd day of December, 2003, by and between **U.S. Bank National Association**, a national banking association, with an address of 141 North Main Avenue, Post Office Box 5308, Sioux Falls, South Dakota 57117-5308 ("Lender") and **Daktronics, Inc.**, a South Dakota corporation, with an address of 331 32<sup>nd</sup> Avenue, Brookings, South Dakota 57006 ("Borrower").

### RECITALS:

- A. Lender and Borrower entered into a Loan Agreement dated October 14, 1998, which Loan Agreement was amended by an Amendment to Loan Agreement dated November 30, 1999, a subsequent Amendment to Loan Agreement dated December 8, 2000, and a Third Amendment to Loan Agreement dated June 20, 2002.
- B. In accordance with the Loan Agreement, Lender is the holder of a Revolving Note dated October 14, 1998 signed on behalf of Borrower. Pursuant to the Amendment to Loan Agreement dated November 30, 1999, the loan amount is \$20,000,000.00 (the "Revolving Loan").
- C. Lender and Borrower mutually wish to extend the maturity date of the Revolving Loan from October 1, 2004 to October 1, 2005.

NOW, THEREFORE, for good and valuable consideration, the parties agree as follows:

1. The Loan Agreement and Revolving Note are hereby amended to provide that the Revolving Loan Maturity Date is October 1, 2005.
2. This Agreement shall not operate as a novation of the Note. Except as modified herein, all of the terms and conditions of the Loan Agreement and Revolving Note, including previous amendments thereto, shall remain in full force and effect.
3. Borrower acknowledges that the Loan Agreement, Revolving Note and related loan documents are and shall remain the legal and binding obligation of Borrower, free of any claim, defense or offset.

U.S. BANK NATIONAL ASSOCIATION DAKTRONICS, INC.

By: /s/ Carl Wynja  
Carl Wynja,  
Vice President

By: /s/ James B. Morgan  
James B. Morgan,  
Chief Executive Officer

By: /s/ William R. Retterath  
William R. Retterath  
Chief Financial Officer

**Daktronics, Inc.**  
**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER REQUIRED BY RULE 13a-14(a) OR RULE**  
**15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO**  
**SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, James B. Morgan, certify that:

1. I have reviewed this quarterly report on Form 10-Q for the quarter ending January 31, 2004 of Daktronics, 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. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) for the registrant and have:
  - a) designed such disclosure controls and procedures or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) disclosed in the report any change in 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;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal controls 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; and

By: /s/ James B. Morgan  
James B. Morgan,  
Chief Executive Officer

Date: February 20, 2004

\* A signed original of this written statement has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

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**Daktronics, Inc.**  
**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER REQUIRED BY RULE 13a-14(a) OR RULE**  
**15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO**  
**SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, William R. Retterath, certify that:

1. I have reviewed this quarterly report on Form 10-Q for the quarter ending January 31, 2004 of Daktronics, 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. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) for the registrant and have:
  - a) designed such disclosure controls and procedures or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) disclosed in the report any change in 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;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal controls 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; and

By: /s/ William R. Retterath  
Daktronics, Inc.  
William R. Retterath,  
Chief Financial Officer and Treasurer  
Principal Financial Officer

Date: February 20, 2004

\* A signed original of this written statement has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

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**DAKTRONICS, INC.**  
**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER PURSUANT TO**  
**SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Daktronics, Inc. and subsidiaries (the "Company") for the quarterly period ending January 31, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, James B. Morgan, Chief Executive Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of 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.

By: /s/ James B. Morgan  
James B. Morgan,  
Chief Executive Officer  
February 20, 2004

\* A signed original of this written statement has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

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**DAKTRONICS, INC.**  
**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER PURSUANT TO**  
**SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Daktronics, Inc. and subsidiaries (the "Company") for the quarterly period ending January 31, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, William R. Retterath, Chief Financial Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of 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.

By: /s/ William R. Retterath  
William R. Retterath,  
Chief Financial Officer  
February 20, 2004

\* A signed original of this written statement has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

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