DAKTRONICS INC /SD/
Form 10-K
June 23, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

[X]**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Fiscal Year Ended April 26, 2008

OR

[ ]**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITES 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	**46-0306862**
(State or other jurisdiction of	(I.R.S. Employer Identification No.)
incorporation or organization)	
201 Daktronics Drive	
Brookings SD	**57006**
(Address of principal executive offices)	(Zip Code)

(605) 692-0200

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: None

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

Title of Each Class	**Name of Each Exchange on Which Registered**
Common Stock, No Par Value	Nasdaq Global Market

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.   Yes[ ] No [X]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.   Yes [ ] No [X]

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[X]   No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.[X]

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

Large accelerated filer   [X]   Accelerated filer   [ ]

Non-accelerated filer   [ ]   Smaller reporting company   [ ]
(Do not check if a smaller reporting company.)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2   Yes[ ]   No [X]

of the Exchange Act).

The aggregate market value of the common stock held by non-affiliates of the Registrant as of October 27, 2007 (which is the last business day at the Registrant's most recently completed second quarter), computed by reference to the closing sales price of the registrant's Common Stock on The NASDAQ Stock Market on such date, was approximately $1,005,946,000. For purposes of determining this number, individual stockholders holding more than 10% of the Registrant's outstanding Common Stock are considered affiliates. This number is provided only for the purpose of this Annual Report on Form 10-K and does not represent an admission by either the Registrant or any such person as to the status of such person.

The number of shares of the registrant's Common Stock outstanding as of June 16, 2008 was 40,388,345.

Documents Incorporated By Reference

Portions of the Registrant's Proxy Statement for its Annual Meeting of Shareholders to be held August 27, 2008 are incorporated by reference in Part III hereof.

DAKTRONICS, INC. AND SUBSIDIARIES

FORM 10-K

For the Fiscal Year Ended April 26, 2008

SPECIAL NOTE REGARDING FORWARD–LOOKING STATEMENTS

This Annual Report on Form 10-K (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 Section 21B of the Securities Exchange Act of 1934, as amended, including statements regarding our 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 with respect to, among other things: (i) our financing plans; (ii) trends affecting our financial condition or results of operations; (iii) our 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 our 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, including those discussed in the section of this Annual Report on Form 10-K entitled "Item 1A. Risk Factors" and "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations – Business Risks and Uncertainties," and those factors discussed in detail in our other filings with the Securities and Exchange Commission.

PART I.

Item 1. BUSINESS

General Development of Business

Company Background and Overview. Daktronics, Inc. was founded by Dr. Aelred Kurtenbach and Dr. Duane Sander in 1968 while they were professors of electrical engineering at South Dakota State University ("SDSU") in Brookings, South Dakota. Our long and close relationship with SDSU and other South Dakota colleges and universities is a key factor contributing to our leadership in the industry. We have been able to experience sustained growth due in part to the capability of the local universities and colleges to provide an important source of highly educated full-time and student employees.

Over the years, our products have evolved significantly, from scoreboards and matrix displays and related software applications to complex, integrated visual display systems that include full color video, text and graphics displays located on a local or remote network and tied together through sophisticated control systems. In the mid-nineties, as light emitting diodes ("LED's") became available in red, blue and green colors with outdoor brightness, we pioneered the development of full color LED video displays capable of replicating trillions of colors, thereby producing large format video systems with excellent color, brightness, energy efficiency and lifetime. Due to our foundation of developing scoring and graphics display systems, in which we were already a leader, we were able to add video capabilities so all of a customer's large format display needs could be met in a complete, integrated system. This has proven to be a key factor in Daktronics becoming the dominant company worldwide in large electronic displays. Over the years, we have invested in product development to add complementary products and services, such as production services, sound systems, marketing services, maintenance and support and other products for our customers.

Business Developments. As a result of our line of LED display systems and software applications, we gained significant market share through designing and manufacturing quality products and providing technical expertise and services. Our products are in use throughout the world, as we are the world's leader in all LED display product categories, according to independent research.

In the sports market, our integrated video and scoring systems have been installed at many professional, collegiate and high schools facilities, particularly in North America, and at international sporting events such as the Olympic games.

With commercial applications, our video, digital billboard and graphics displays can be seen in major destination sites, such as Las Vegas and Times Square, along roadsides at retail establishments and at many other locations.

In the transportation market, our Vanguard® displays are in use in numerous jurisdictions across North America and our customers include many state departments of transportation.

One of our core growth strategies has been to enter geographic markets by developing a small sales and service presence that provides after-sale support to our entire product line and sales of our products. This network of offices, including home offices, has historically been and is expected to continue to be an important part of our growth strategy. We currently have approximately 60 corporate offices throughout the world.

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We occasionally acquire businesses that provide access to new markets or complement our existing products. In the past five years, we have acquired a number of small companies. Although these acquisitions increased the scope of services and technology that we are able to provide, our primary growth objective is still the increase of sales through organic growth.

Financial Information About Segments

See Note 2 of the Consolidated Financial Statements for financial information pertaining to our business segments and geographic operations.

Narrative Description of Business

We are the world's leading supplier of electronic scoreboards, large electronic display systems and related marketing services, digital messaging solutions, software and services for sports venues, commercial and transportation applications. Our continuing focus is on supporting customers with superior products, integration and services that provide dynamic, reliable and unique visual communication solutions. We offer a complete line of products, from small indoor and outdoor scoreboards and electronic displays to large multi-million dollar video display systems as well as related control, timing, sound and hoist systems and related professional services. We are recognized worldwide as a technical leader with the capabilities to design, market, manufacture, install and service complete integrated systems that display real-time data, graphics, animation and video.

We are engaged in a full range of activities: marketing and sales, engineering and design, manufacturing and professional services. Each of those activities is described below.

Marketing and Sales. Our products have been sold throughout the United States and other countries through a combination of direct sales personnel and resellers. In the United States and Canada, we use primarily a direct sales force for professional sports, colleges and universities, convention centers and smaller sports facilities, including high schools and transportation applications. In smaller commercial applications, we rely primarily on resellers. We also utilize resellers outside North America on large video system projects where we do not have a direct sales presence. Sales to resellers generally have terms equal to sales directly to end users.

The majority of the products sold by resellers are standard catalog products. These are typically moderately priced and relatively easy to install. A limited number of models are built to inventory and available for quick delivery. We support our resellers through direct mail advertising, trade journal advertising, trade show exhibitions and our sales force support in the field. We believe that we can expand sales and in some niches, market share, by expanding both our direct sales force and resellers.

Our direct sales force is comprised of a network of offices located throughout the world supporting all customer types in both sales and service. In addition to supporting resellers as described above, the direct sales staff sells the entire range of our standard products and substantially all of the large video display systems. Our direct sales staff is structured in a way to maximize cross-selling opportunities across segments. We have organized our business into five business units which have a primary focus on particular markets and a secondary focus on opportunities in other markets. The business units consist of four domestic business units that include U.S. and Canada: Commercial, Live Events, Schools and Theatres, and Transportation and a fifth business unit for international operations. We believe that customers in each area are unique in a number of ways which are conducive to this structure. For example, live events customers usually have a large variety of products tied into a system in a single location that involves much more creative production services, design and event support. The Commercial business unit relies more on needs created by large and remote networks of displays connected through various modes of communication. The Transportation business unit focuses on the unique needs of governmental contractors and ties into integrated systems that manage the flow of travelers and vehicles. Finally, the Schools and Theatre business unit focuses on the increasing level of support and service and limited resources along with all the statistics and related software and communication needs of athletic conferences and leagues.

When we target a potential customer for sales opportunities, the prospect is contacted either directly or through a reseller. Frequently, on larger sales opportunities, engineers, technicians and sales personnel jointly participate in site visits to assess site conditions, evaluate the customer's requirements and assemble and present proposals. Proposals to prospective customers include business and technical presentations as well as product demonstrations and visits to existing installations. We also regularly host customers at our various manufacturing facilities to demonstrate product quality, manufacturing, and design capabilities.

International sales fluctuate from year to year based on the timing of large system projects. A typical term of sale for international projects includes a letter of credit or partial payment in advance. We believe that in addition to the growth we expect domestically, we will also achieve growth in the international markets. During fiscal years 2008, 2007 and 2006, approximately 13%, 10% and 10% of our net sales, respectively, were derived from international sales. Since 2000, we have acquired or opened international offices in Canada, China, France, the United Arab Emirates, Germany, Australia and the United Kingdom. We also are a 49% owner of a joint venture in Malaysia.

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Much of our marketing and sales success in the past was based on our ability to create new products and product enhancements for customers by understandingtheir needs and opportunities. We have developed and continue to develop this understanding through active participation in the sales cycle by engineers and other personnel and through attendance at trade shows, conventions and seminars and fostering a culture of teamwork throughout the organization.

Engineering and Product Development. The large screen electronic display industry is characterized by ongoing product innovations and developments in technology and complementary services. To remain competitive, we must continue to anticipate and respond to changes and developments in the industry. We will continue our tradition of applying engineering resources throughout our business to help achieve more effective product development by investing approximately 4% of our net sales into product design and development.

We employ engineers and technicians in the areas of mechanical and electrical design, applications engineering, software design and customer and product support. We use primarily in-house engineering to anticipate and respond rapidly to the product development needs of customers and the marketplace. We assign product managers from our engineering staff to each product or product family to assist our sales staff in training, implement product improvements, and ensure that each product is designed for maximum reliability and serviceability. We also invest in new creative technologies and in companies developing new technologies.

Our engineering staff consists of four product development groups – Sports, Video, Commercial and Transportation. The Sports Product development group focus is aligned with the Schools and Theatre business unit, the video group is aligned with the Live Events and International business units and the commercial and transportation groups are aligned with the Commercial and Transportation business units.

Until fiscal year 2008, each engineering group was autonomous to allow it to focus on one product family. Beginning in fiscal year 2008, we implemented a more matrix-based organization with key leaders of each engineering group being responsible for design initiatives across all groups. This allows us to take advantage of core technologies that can be used across product categories. We believe that this is a core strategy to drive the highest quality and most reliable products.

Manufacturing. As a vertically integrated manufacturer of display systems, we perform most sub-assembly and substantially all final assembly of our products.

Our manufacturing operations include component manufacturing and system manufacturing (metal fabrication, electronic assembly, sub-assembly and final assembly). We augment our production capacity with the use of outside resources primarily due to capacity constraints,

although we have also used outside providers when it was more cost effective.

We use a modular approach for manufacturing displays. Standard product modules are designed to be used in a variety of different products. This modular approach reduces parts inventory and improves manufacturing efficiency. We inventory a limited supply of standard products. Custom projects are built according to the customer's specifications. Product modules are designed so that a custom product may include a significant percentage of standard components to maximize reliability and ease of service. A key strategy of ours is to reduce the need for customization of displays and increase standardization. For example, we are developing a more widespread use of a common module platform and are expanding use of a standard formed cabinet for displays.

Our order entry, production, customer service and many other functions are also consolidated through an enterprise resource planning system to facilitate communication among employee teams throughout the entire sales, design, production and delivery process.

During fiscal year 2006, we began significant expansion of our facilities and throughput to respond to the increasing level of sales. Prior to that time, substantially all of our products were manufactured in our main facility in Brookings, South Dakota. During fiscal year 2007, we began manufacturing in Sioux Falls, South Dakota and Redwood Falls, Minnesota. We also deployed a limited amount of manufacturing in China and expect to expand that location in the upcoming fiscal year. Locations outside of Brookings now produce a material amount of our products.

During fiscal year 2007, we began reorganizing our plants to more closely align them with the five business units described above. In the fourth quarter and fiscal year 2008, we deepened this reorganization by allocating inventory and decentralizing various other functions to each plant. This resulted in significant investment in replicating processes which in prior years were centralized. This was extremely important given the rapid growth of the business and the resulting unique needs of our customers in each business unit. Our goal is to align sales, marketing, engineering and manufacturing into a cohesive business unit with a focus on customers while not giving up the synergies of shared resources. In addition, given the cyclical nature of some parts of our business, we need to maintain our ability to manufacture the same products across our plants so that we can smooth out the peaks and valleys of customer demand of the various business units.

Technical Contracting. We serve as a technical contractor for larger display system installations that require custom designs and innovative product solutions. The purchase of standard displays and other state-of-the-art display systems typically involves competitive proposals. As a part of our response to a proposal request, we may suggest additional products or features to assist the prospective customer in the optimal type of display

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system. We usually include, as a part of our proposal, site preparation and installation services related to the display system. In these cases, we serve as a contractor and may retain subcontractors. We are licensed in a number of domestic jurisdictions as a general contractor. Generally, we outsource all related electrical, steel and installation labor to qualified subcontractors with which we have developed relationships.

Professional Services. Our professional services are essential to continued market penetration and growth. We provide maintenance and support services and technical contracting in all of our offices throughout the world. We are currently evaluating our office network in the U.S. to ensure that the organization is functioning efficiently from a cost perspective. This includes reevaluating the need for offices in certain locations, our current approach to parts logistics and various other matters. We supplement our offices with a network of authorized service companies for

service and maintenance needs.

Professional services we provide in addition to technical contracting include event support, content creation, product maintenance, marketing assistance, training on hardware and software, and display rentals. Our creative production staff provides a variety of services to customers, including video content, event support, control room design, on-site training (hardware and software), and continuing technical support for operators of complicated display systems.

Our sports marketing division provides customers with marketing and ad sales for facilities to fund display system purchases. These marketing services extend beyond the marketing potential of the equipment in the facility to other facility-related components. Typically, we render these services to facilities that do not have in-house marketing programs and staff.

Customer Service and Support. Our customer service distinguishes us from our competitors. This service includes limited warranties for most of our products against failure due to defective parts or workmanship for periods generally ranging from one to five years after the first sale or installation, depending on the product or type of customer and extended service agreements. We also provide help-desk access, parts repair and replacement and programming support for video, animation and other displays. We staff our help desk with experienced technicians who are available on-call 24 hours a day to support events and sites.

Our repair center is staffed with trained technicians who repair and return components that require service, and we offer a component exchange program for same-day shipment of replacement parts.

Beginning in fiscal 2009, we reorganized our North American field service personnel so that we could better focus on the commonality of the products across units rather than the unique customer needs, which was the prior focus. We believe that we can drive significant cost savings and synergies by doing this that will become visible as we enter into the second half of the fiscal year.

General Description of Our Products and Technologies

Our display technologies have changed significantly since the mid-1990s when incandescent lamps were the primary display element. Presently, LED and liquid crystal display ("LCD") technologies are the primary display elements. The invention and availability of the blue and green LED in the mid-1990s, along with the already available red LED, allowed the introduction of full-color video displays using LEDs as the primary colors to form all other colors in the video display. The decreasing costs of LCD components along with the drive for more numerous smaller displays have led to the addition of LCD displays. Driven by customer demand, we have enhanced our video display technology into mobile and modular technologies and high definition capabilities for various applications.

The cost, performance and availability of LEDs has made them the preferred display element for large displays as compared to alternatives such as incandescent and reflective technologies, most of which are obsolete or unproven. The cost effectiveness, life and performance of LCDs have made them the preferred small display solution. The vast majority of displays we sell today utilize LED technology.

The two principal components of many of our systems are the display and the controller. The controller uses computer hardware and software to process the information provided by the operator and other integrated sources and then compiles the information, graphics or animation to be presented on the display. Data can be transferred between the controller and local or remote displays. Local connections may use wire cables, fiber optic cables, infrared links or radio links. Standard and cellular telephone connections and satellite transmissions are used to connect to remote displays. The controller controls each of the pixels (which are the dots or picture elements that make up the image) on the display to present the message or image.

Most of our display technologies rely on one or more of our software products to manage and provide content for the display. These software products range in complexity from scoring consoles, to the Venus® 1500 control software that allows the creation, display and scheduling of dynamic text and basic graphics content on electronic displays, to the Venus® 7000 display control system that controls multi-color displays and video displays, providing the ability to create graphics and animation as well as interfacing with third-party software for content. Additionally, our Visiconn^{SM} control software is used to display targeted messages to specific

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audiences and to control large networks of digital displays. Complementary software, such as our DakStats® and interfacing software, is also available and can be fully integrated into the control software.

Our display systems range from small scoreboards and digit displays priced at under $1,000 to large complex display systems priced in excess of $20 million. Generally, our product sales are either custom products or standard catalog scoreboards or displays. Historically, these standard catalog sales have accounted for less than 25% of our total annual revenues. Our custom products are customized in terms of size, configuration and installation type but are generally built using standard technology platforms. In 2008, we initiated various programs to reduce custom components in favor of much more standardized components that could be assembled and put together to form products that in the end are customized to the needs of the end users.

Within each product family, we produce displays that vary in complexity, size and resolution. The physical dimensions of a display depend on the size of the viewing area, the distance from the viewer to the display, and the amount and type of information to be displayed. Generally, the light source, or pixels, are larger and spaced farther apart for longer distance viewing. The type of the display may also depend on the location of the viewing audience. For example, arena scoreboards may have a viewing angle nearly as wide as 180 degrees, compared with roadside displays, which typically are viewed from a passing vehicle only within a narrow angle from the display. We customize our products according to the design specifications of the customer and the conditions of the environment.

Product Families and Technologies

Our products are comprised of the following five major product families:

1. Sports products, primarily All Sport®, Tuff Sport® and OmniSport® scoreboards, Sportsound®
   sound systems and related controllers and products;
2. Automated rigging and hoist products, primarily our Vortek® line of hoists and related control systems;

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3.   Video products, primarily HD-X, ProStar®, ProTour® and ProAd® displays and associated control systems;

4.   Commercial products, primarily Galaxy® and Valo™ displays and Venus® 1500 control systems; and

5.   Transportation products, primarily Vanguard® displays.

Each of these product families is discussed below.

Sports Products. The sports products family includes a full line of indoor and outdoor scoreboards, timing systems, digit displays, sound systems, statistics software and other related products. The indoor products range in complexity from two-digit shot clocks and small scoreboards to large, center-hung scoreboards incorporating message centers, advertising panels and hoist systems. Outdoor scoreboards range in complexity from two-digit game timers and small scoreboards to large scoring systems incorporating message centers and advertising panels.

We expect that sports products sales in the future will continue to focus on the use of LED technology due to its lower power consumption, longer life and resulting lower maintenance costs as compared to other technologies. Because most of the products within the sports products group have significant standardization, we have been able to make progress on our goal of delivering the highest quality products while maintaining consistent margins.

We offer a variety of internally developed controllers complementing our scoreboards and displays. These controllers vary in price and complexity from the All Sport® 100, which is a controller for portable scoreboards, to the All Sport® 5500, which is designed for more sophisticated scoring systems, allowing for more user-defined options. These controllers can be interfaced with the scoreboards through radio frequencies, fiber optic connections or other means.

We also offer timing systems for sports events, primarily aquatics and track competitions. These timing systems include our OmniSport® 2000 timing system. The system has the capability to not only time and rank the competitors but also to interface to event management software created by other third parties to facilitate the administration of the sporting event.

As a key component of an integrated system, we market sports statistics and results software under the DakStats® trademark. The software allows entry and display of sports statistics and other information displays. It is one of the leading applications of its type in professional, collegiate and high school sports.

Automated Rigging and Hoist Products. The automated rigging and hoist product family includes our Vortek® automated rigging systems which complement our arena center-hung scoreboard/display systems for both small and large sporting facilities. Additionally, the Vortek® hoist provides automated rigging for theatre applications, primarily smaller theatres such as in high schools and similar venues. The strengths of the Vortek® automated rigging systems include safety and ease of operation.

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The Vortek® Automation Center includes intuitive touch screens and menus to control the integrated hoist systems in a central control system to provide for added safety and enhanced operation of a theatre production, making changes in scenery, lighting and sound preprogrammed, timed

and easy to control.

We also offer custom hoists, primarily in the sports arena business, for all sizes of center-hung video and scoring solutions. These custom hoists, which are designed to the specifications of the center-hung structure and the load and design features of its attachment points within a facility, provide the most capable and proven systems in the industry.

Video Products. The video products family consists primarily of displays, which are comprised of a large number of pixels capable of creating various levels of video, graphics and animation, and controllers, which manage the operation of the display. Video display products are based on red, green and blue LEDs arranged in various combinations to form pixels or picture elements. The electronic circuitry which controls the pixels allows for variances in the relative brightness of each LED to provide a full color spectrum, thereby displaying video images in striking, vibrant colors.

We offer a wide range of video display products for different applications and budgets. Variables in typical video displays include the spacing of the pixels (pixel pitch), the brightness of the displays, the number of discrete colors that the display is able to produce (color resolution) and the viewing angle. In addition, modular design allows the product to be readily configured in custom sizes to meet each customer's specific requirements, with no maximum to the size of display that can be built.

Our ProStar® and HD-X video display systems offer specifications second to none in the industry. At the high end, the product is capable of producing 4.4 trillion colors and is available with pixel spacing as close as three millimeters. Currently, we offer a wide range of pixel spacing, ranging from three millimeter to 89 millimeter. The three-millimeter application provides the user with the greatest pixel density and shortest viewing distance, and the 34-millimeter is the most cost effective for physically large displays with maximum viewing distances. In addition, the uniformity of colors across the display is important to the quality of the video image. Our unique display control circuitry along with our proprietary manufacturing and calibration procedures provide uniform colors across the display.

We have adapted our ProStar® technology into our ProAd® digital advertising and information display system, the ProTour® modular display system, the ProRail® display systems and our ProPixel™ display systems. ProAd® technology uses red, green and blue LED modules configured in different height-to-width ratios to give arena and stadium facilities the ability to install long, narrower bands of displays in various locations in the facility. This application generally serves as a revenue generation source for facilities through advertising as well as a location to display information such as scoring and statistics.

ProTour® display systems are comprised of lightweight individual modules or panels less than a square meter in size that are assembled together to form a display in a customizable height and width. These panels are used in what we refer to as mobile and modular applications, such as touring shows and the events market. ProRail® display systems incorporate our ProAd® displays into a patented cabinet designed to serve as a replacement for the fascia of an upper deck in a stadium or arena, which in some cases saves construction costs and improves the sight lines of the fans. ProPixel™ displays serve as architectural accents and channel lettering.

Our main controller for these video displays is our Venus® 7000 controller, which is built on the Windows® operating system. This high-end controller provides advanced capability for controlling large video displays. The V-Play® event management software provides facilities with integrated and sophisticated event program management capabilities with integration to video equipment. It provides instant replays, live action and overlays of information and it allows for the organization and playback of digital video and audio clips. Other video products controllers include the Visiconn℠ and V-Tour® controllers. Each of these controllers is designed with unique features and functionality for unique market niches.

Our V-Tour® design interfaces between our display systems and other systems allowing, for example, scoreboard and video systems to receive and display information from computers used for statistics, timing or scoring. These interfaces allow the display controller to send information back to a statistics system or customer computer and can automatically report continually updated sports scores and information from national wire services.

Commercial Products. The key product lines in the Commercial Products family are our Valo™, Galaxy® and GalaxyPro™ product lines, which include various indoor and outdoor applications intended primarily as graphics and text-based displays.

Galaxy® displays, available in both indoor and outdoor models, are our leading product line for commercial applications and are expected to be a key product line for growth in the future. Galaxy® displays are red, amber or full color, with pixel spacing ranging from 7.6 millimeter to 89 millimeter depending on size and viewing distance. They are used primarily as message centers to convey information and advertising to the consumers and the public. The modular design of the product allows us to configure a display to readily meet the size requirements of each customer. Within the Galaxy® line, we offer various price points for similar sized displays of the same pixel spacing.

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GalaxyPro™ displays are full-matrix outdoor displays capable of displaying pre-recorded video, text, graphics and animation. GalaxyPro™ displays are offered in full color with pixel spacing from 20 millimeter to 34 millimeter. GalaxyPro™ displays are capable of producing 68 billion colors, have excellent color uniformity across the display and are fully compatible with our Venus® 1500 display control software. The modular design of the product allows us to configure a display to readily meet the size requirements of each customer.

Our Valo™ displays, used primarily in the digital billboard marketplace, utilize the foundation of our ProStar® technology to create a unique digital display product for outdoor advertisers. The product, which is used primarily to display static images that change at regular intervals, include many features and functionality that are unique to the outdoor advertising business, such as our patented mounting system, self adjusting brightness, improved energy consumption, and network security.

Other product lines within the Commercial Products group include our DataTime®, DataMaster®, DataTrac™ and DakTicker® displays. The DataTime® product line consists of outdoor time and temperature displays in various character sizes. The DataTime® displays feature a programmable time and temperature display and use a remote sensor for temperature data input. The DataMaster® product line consists of outdoor rate, gas price, generic counting/timing and lottery displays in various character sizes. The DataTime® products are offered in red or amber, while the DataMaster® products are offered in red, amber and green. The DataMaster® product line has growth potential in the petroleum market niche.

The DataTrac™ product lines consist of indoor LED displays comprised of discrete characters. Each character is spaced evenly horizontally and vertically from the adjacent character. This provides the least expensive display per character for the display of text messages only. DakTicker® displays are used primarily in financial institutions for ticker displays and to display other financial information. DataTrac™ and DakTicker® products have a controller in the display that is capable of receiving a downloaded display program and then operating independently to display that program until a new program is downloaded to it.

The majority of our Commercial Products group's products utilize our proprietary Venus® 1500 display control software to control the creation of messages and graphic sequences for downloading to the display. This software is designed to be useable without any special training, and it is applicable to all general advertising or message presentation applications. We also provide software that allows system integrators to write their own software using the Venus® 1500 software developer's kit to communicate to displays supplied by us. Several system integrators have implemented the Venus® 1500 protocol into their specific applications, resulting in additional display sales. Our Valo™ display line utilizes the Valo™ Play control system to manage the operation and content of displays on a networked basis.

Transportation Products. The Transportation Products family includes a wide range of LED-based products for road management, parking, mass transit and aviation applications. The Vanguard® family of electronic displays, which lead transportation product sales, are typically used to direct traffic and inform motorists. The Vanguard® line includes both permanently mounted and portable displays. We have also developed a software control system for these displays to help transportation agencies manage large networks of displays.

Our digit and directional displays are primarily marketed under the DataMaster® name and sold for use in parking facilities. Several of the transportation products are also routinely sold into our commercial and sports markets.

Most of the transportation products are designed and tested to rigorous transportation industry standards. Our personnel routinely work with standards development organizations to assist in writing standards that benefit the public and take advantage of the latest display technologies.

Sources of Raw Materials

We source some of our raw materials, including LEDs, from a limited number of suppliers, primarily due to quality control or the customized nature of the materials. The loss of one of these key suppliers could have an adverse impact on our business and operations. For additional information, refer to Item 1A – Risk Factors. From time to time, we enter into pricing agreements or purchasing contracts under which we agree to purchase a minimum amount of product in exchange for guaranteed price terms over the length of the contract, which generally does not exceed one year.

Intellectual Property

We develop technology on a continuing basis that we consider for patent application. We apply for the majority of our patents to establish the creation of the technology so that other parties cannot later claim ownership. We generally do not pursue infringement claims on these patents when others infringe on them. The remainder of our patents are designed to prevent infringement, and we aggressively pursue infringement claims for protection due to patent violations.

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We apply for patents in the U.S. and a limited number of foreign jurisdictions. These patents generally pertain to our display technologies and product features and have various terms of duration. The patents we hold which are designed to protect and prevent competitors from infringing include, for example, patents on mechanical designs such as our ProRail® system and our Valo™ Mount, our ProStar® formed cabinet and our

latching system for modules. They also include patents for product features and capabilities which we believe are superior in the marketplace and that give us a competitive position, such as our touchpad products for aquatics. There are a limited number of patents that apply to our electronics due to the rapid rate of change in the industry. However, we hold patents on such things as calibration methods and pixel arrangements. Due to the general nature of our business and the rapid rate of change in technology, we do not incur significant expenditures in defending or prosecuting patent claims.

We rely on trademarks, in addition to patents, to help establish and preserve limited proprietary protection for our products. Our trademarks are registered in the United States and other countries. We also have numerous trademark applications pending. These trademarks are used to establish brand recognition and distinction in our various markets.

Product drawings, software, training and product manuals and other works of authorship are also subject to applicable copyright law protections. We provide software to our customers in object code to help preserve our intellectual property rights. We also rely on nondisclosure and license agreements with our employees. Despite these intellectual property protections, there can be no assurance that a competitor will not copy the functions or features of our products.

Seasonal Nature of the Business

Our sales and profitability historically have fluctuated due to the impact of large product orders, such as display systems for facilities where professional and major college sports events take place and large commercial systems and networks. The seasonality of the sports market has also played a part in our sales and profit fluctuations. As a result, sales and net income in the first and second quarters of a fiscal year tend to be higher than in the third quarter of a fiscal year, followed by higher levels in the fourth quarter leading into the first quarter of the following year.

The seasonality of the sports business is caused by sales related to facilities for football in the summer and early fall, followed by sales generally related to facilities for basketball and hockey in the fall, and finally facilities for baseball in the early to late spring. This seasonal effect is generally compounded by large product orders in the sports markets and by the effects of holidays during the third quarter. The effects of seasonality unrelated to holidays are generally not found in our Commercial, International and Transportation business units, although the impact of large orders in those markets can cause significant fluctuations in sales and profits. We believe that with the mix of business favoring more emphasis on outdoor advertising applications, we could see more seasonality in the Commercial business unit in the future, with sales slowing in our winter months. Approximately 46% of our net sales are in the Schools and Theatres and Live Events business units, 36% are in the Commercial business unit, 10% are in the International business unit and the remaining approximately 7% are in the Transportation business unit.

Gross margins on large orders tend to fluctuate more than the gross margins on smaller orders. Large product orders that involve competitive bidding and substantial subcontract work for product installation generally have lower gross margins with greater variability in margins. Although we follow the percentage of completion method of recognizing revenues on the majority of these larger orders, we nevertheless have experienced fluctuations in operating results and expect that our future results of operations will be subject to similar fluctuations.

Working Capital Items

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. We often receive down payments or progress payments on these orders. To the extent

that these payments are not sufficient to fund the costs and expenses associated with these orders, we use working capital and bank borrowings to finance these cash requirements.

Customers

The primary markets we serve, along with types of customers, are as follows:

Markets	**Types of Customers**
Live Events	Large colleges and universities, professional sports teams and facilities, Olympic games, national and international sports federations, civic arenas and convention centers, staging and rental, and motor racing.
Schools and Theatres	