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# Financial Analysis and Valuation of Daktronics Inc.

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## Daktronics Inc.

DAKT / NASDAQ GS

Initiating Coverage

Investment Rating: Hold

Price: USD 7.45 S&P 500: 2,834.4 DJIA: 25,928.68 RUSSELL 2000:1,539.74

- Daktronics faces challenges from current global tariff and trade environment.
- Sales are expected to grow.
- Order bookings remain strong.

Valuation	2019 A	2020 E	2021 E
EPS	0.29	0.28	0.28
P/E	19.9	21.7	22.7
CFPS	\$0.35	\$0.61	\$0.65
P/CFPS	17.65	10.67	10.47

Market Capitalization	Stock Data	
Equity Market Cap (USD):	336,243,000	52-Week Range (USD): 7.14-10.11
Enterprise Value (USD):	265,400,000	12-Month Stock Performance: 9.5
Shares Outstanding:	45,013,000	Dividend Yield: 3.76%
Estimated Float (M):	36.97	Book Value Per Share (USD): 4.47
3-mo Avg. Daily Volume (M):	2.56	Beta: 0.9



### Company Quick View:

**Location:** 201 Daktronics Dr, Brookings, SD 57006-5128

**Industry:** Signs and Advertising Specialties (SIC 3993) / Sign Manufacturing (NAICS 339950)

**Description:** Daktronics, Inc. and subsidiaries is the world's largest supplier of large screen video displays, electronic scoreboards, LED text and graphics displays, and related control systems, services and products. The company was founded in 1968 and is based in Brookings, South Dakota.

**Key Products & Services:** The main products include large screen video displays, electronic scoreboards, computer programmable displays, digital billboards and control systems.

**Website:** <http://www.daktronics.com>

**Analyst:** Rakshya Shrestha

## STOCK PRICE PERFORMANCE

The figure below depicts the 5-year stock price performance of Daktronics, which displays that the stock price of Daktronics has been decreasing. The one-year capital gains for Daktronics' stock between March 31, 2018 and March 29, 2019 is -9.59 percent and the annualized gain is -9.70 percent.

**Figure 1: 5-year Stock Price Performance**



The stock price of Daktronics has been decreasing from 2014, however it has remained relatively constant through 2018 and beginning of 2019 with closing price of USD 7.45 on March 29, 2019. Daktronics Inc.'s competitor LSI Industries, Inc. (LYTS) has total annual return of -63.67 percent. The stock price of LSI has also been decreasing since 2016 with a closing price of USD 2.63 as of March 29, 2019. Looking at the returns, Daktronics has been noticeably doing better than its competitor.

The Russell 2000, an index used as a benchmark for small-cap stocks in the U.S., shows a total return of 4.65 percent for the period of March 31, 2018 to March 29, 2019. Daktronics' has lower total return compared to Russell 2000.

Part of this price behavior of Daktronics is because of external variables such as the economy and part due to company-specific events during the year. Daktronics is facing challenges because of current trade environment and global trade tariffs that has created cost headwinds on commodity and components used in the production process.

However the company's order booking system is strong as the orders for commercial and live events are up for the year and show promising future for Daktronics.

## **COMPANY DESCRIPTION**

Daktronics, Inc. is the world's largest supplier of large screen video displays, LED text/graphic displays, electronic scoreboards and related control systems, services and products. Aelred Kurtenbach and Duane Sander, professors of electrical engineering at South Dakota State University founded Daktronics Inc. in 1968 in Brookings, South Dakota. The company originated with the design and manufacture of electronic voting systems for state legislatures. However today Daktronics, Inc. and its subsidiaries are primarily involved in the design, market, and manufacture of a wide range of integrated electronic display systems and related products for sporting, commercial and transportation applications that are sold worldwide. The company offers products and services ranging from small scoreboards and electronic displays to large multimillion-dollar video display systems as well as related control, timing, and sound systems.

Daktronics, Inc. became a publicly traded company in 1994, offering shares under the symbol DAKT on the NASDAQ. As of June 4, 2018, Daktronics Inc. has 1,045 shareholders of record. Currently Daktronics has its headquarters in Brookings, SD, with other facilities in Sioux Falls, SD, Redwood Falls, MN, Shanghai, China, and Belgium, along with more than 50 regional offices around the world.

Daktronics focuses on the following product families, all of which include control systems and software:

- Video displays
- Scoreboards and timing systems
- Message displays
- ITS (intelligent transportation systems) dynamic message signs
- Space availability displays
- Audio systems
- Out-of-Home advertising displays
- Digit and price displays
- Indoor dynamic messaging systems

The company is engaged in full range of activities such as marketing and sales, engineering and product design and development, manufacturing, technical contracting, professional services and customer service and support. The business is organized into five segments: Commercial, Live Events, High School Park and Recreation, Transportation, and International. The mission of Daktronics is to be the world leader at informing and entertaining audiences through dynamic audio-visual communications systems. To acquire this mission the company aims to provide quality products for long-term success and strive to win replacement business from existing customers.

According to independent market research firm iSuppli Corp. Daktronics Inc. has approximately 30 percent of the entire worldwide LED video display market share. Daktronics holds or own licenses to use numerous patents, copyrights, and trademarks on a global basis. Since its incorporation Daktronics has acquired seven organizations. Their most recent acquisition was in June 2018, where Daktronics acquired AJT Systems Inc.'s services and technology to expand the company's control system features and offerings. With this acquisition the company expects to add additional offerings and services to the entertainment for live events customers through the integration of broadcast-style graphics, including real-time live to air graphics rendering and video server systems.

## **MANAGEMENT PERFORMANCE AND BACKGROUND**

Daktronics has five key executives that lead the company. The executive team members of Daktronics Inc. are listed in Table 1.

**Table 1: Executive Team of Daktronics**

<b>Name</b>	<b>Position</b>
Reece A. Kurtenbach	Chairman, President, Chief Executive Officer
Bradley T. Weimann	Executive Vice President
Carla S. Gatzke	Vice President, Corporate Secretary
Matthew John Kurtenbach	Vice President, Manufacturing
Sheila Mae Anderson	Chief Financial Officer, Treasurer

*Source: Yahoo Finance*

Reece A. Kurtenbach was appointed as President and Chief Executive Officer and a Director for Daktronics, Inc. in 2013 and currently also serves as Chairman of the Board of Directors. He is the son of Dr. Aelred Kurtenbach, one of the founders of Daktronics. He joined the company in 1991 as an Applications Engineer focusing on large display projects. Bradley T. Wiemann has been an Executive Vice President of Commercial and Transportation at Daktronics Inc. since June 15, 2012. His responsibilities include sales and service for High School Park and Recreation business unit. Carla S. Gatzke has been Corporate Secretary and Vice President of Human Resources at Daktronics Inc. since 1994 and 2006 respectively.

Matthew John Kurtenbach has been Vice President of Manufacturing at Daktronics Inc. since 2006. He is responsible for repair center operations associated with after-sales services and also lead the company's transformation to lean manufacturing. Sheila M. Anderson serves as Chief Financial Officer (CFO) and Treasurer of the company since September 2012.

### **Board Of Directors**

There are currently seven individuals on the Board of Directors of Daktronics, which is divided into three classes serving three-year terms. The seven-member board consists of one female and six male members. Current committees include Audit, Compensation, and Nominating and Corporate Governance. The complete list of board members is included in Table 2.

The Nominating and Corporate Governance Committee has determined that Anderson, Mulligan, Dutcher, Friel, Morgan and McDermott and Frame are "independent," as that term is defined in Rule 5605(a)(2) of the NASDAQ Listing Rules. Accordingly, the Board is composed of a majority of independent Directors as required by the NASDAQ Listing Rules. It can be seen from the table below that Reece A. Kurtenbach holds the position of President, Chairman of the Board as well as Chief Executive Officer (CEO) and it is advisable that the CEO and Chairman be different persons. Daktronics has yet to adhere to this advice.

**Table 2: Daktronics Inc.'s Board of Directors**

Reece A. Kurtenbach	President, Chairman of the Board and Chief Executive Officer
Byron J. Anderson	Director, Compensation Committee and Nominating and Governance Committee Member
Robert G. Dutcher	Director, Compensation Committee Chairman
Nancy D. Frame	Director, Lead Independent Director and Nominating and Corporate Governance Committee Chairperson
John Friel	Director, Audit Committee and Nominating and Corporate Governance Committee Member
Kevin P. McDermott	Director, Audit Committee Chair
James B. Morgan	Director, Audit Committee and Nominating and Corporate Governance Committee Member

*Source: Daktronics Inc.'s website*

With regards to management incentives, Daktronics has a Compensation Committee, which administers equity-based compensation and management incentive programs, and other compensation initiatives identified by the Board. The Compensation Committee also reviews and approves each executive's base pay, bonus and equity incentives annually. The committee also undertakes and reports management succession planning to the CEO and the Board.

## **PEER ANALYSIS**

Daktronics Inc. faces a broad variety of competitors that appear both from within the United States and foreign companies that range in size and product offerings. Some competitors compete in certain markets by providing lower-cost display systems, which are of a lesser quality with lower product performance or include less customer support. Other competitors use sponsorships as a means to win the business at a location.

Daktronics Inc.'s SIC code is Signs and Advertising Specialties (3993) and NAICS code is Sign Manufacturing (339950). The SIC and NAICS codes of Daktronics Inc. is very broad and many competitors vary by product, location and business unit. In addition to that there are some competitors in the market such as Young Electric Sign

Company (YESCO), Watchfire Signs LLC and Nano lumens that are privately owned and/or do not have financial data accessible for the general public. Because of such limitations, I have enlisted LSI Industries and Brady Corporation: Signmark Division as the main competitors based on the SIC and NAICS codes and company size which relate most to Daktronics.

### **LSI Industries Inc. (LYTS)**

LSI Industries (NASDAQ: LYTS) is headquartered in Cincinnati, Ohio and is known for developing superior image solutions through world-class lighting, graphics, and technology capabilities. It makes visual displays and graphics, which are purchased primarily by gas stations and convenience stores. LSI is a vertically integrated U.S. based manufacturer with a focus on serving customers in North America and Latin America. LSI has facilities in Ohio, Kentucky, California, New York, North Carolina, Rhode Island and Texas. The Company's common shares are traded on the NASDAQ Global Select Market under the symbol LYTS.

### **Brady Corporation: Signmark Division (BRC)**

Brady Corporation's product line include do-it-yourself printing systems, labeling materials, signs and software, spill control and regulatory compliance devices. Since the company is a specialty business-to-business manufacturer, its products are rarely obvious to the general public. The company's products are mainly used inside manufacturing facilities, public buildings, computers, airplanes, and mobile phones. Brady Corporation is headquartered in Milwaukee, Wisconsin. It went public and began trading on the NASDAQ market since 1984.

Table 3 provides comparisons of Daktronics with its relevant peers.



**Table 3: Peer Analysis Relevant Comparisons**

Company	Ticker Symbol	Market Cap (In Millions)	PE Ratio	P/BV	EV/ EBITDA	Debt/ Assets	ROA %	ROE %
Daktronics	DAKT	372.342	55.4	4.4	27.35	0.44	2.06	3.67
LSI	LYTS	86.987	N/A	5.37	(5.97)	0.39	(9.43)	(15.55)
Brady Corp	BRC	2528.00	26.7	15.36	14.36	0.049	8.6	12.1

Source: Yahoo Finance, NASDAQ as of February 23, 2019

Daktronics has a market cap between that of LSI and Brady Corp. Its debt to asset ratio is high compared to LSI's and Brady's ratios. Daktronics has the highest EV / EBITDA multiple.

### ROIC Comparison

Table 4 displays Daktronics and their main competitor's return on invested capital (ROIC). ROIC is a profitability ratio that measures how a company is efficiently using investors' funds to generate income.

**Table 4: Daktronics vs. LSI ROIC Comparison**

Year	Daktronics ROIC (%)	LSI ROIC (%)
2018	2.75	-8.94
2017	5.22	2.35
2016	0.44	6.94
2015	8.69	3.90
2014	9.80	0.67

Source: Own Calculations

The results above show that except for the year 2016 the ROIC for Daktronics is higher compared to LSI, which indicates that Daktronics is performing better than the competitor in converting investor capital into profits. However, most likely, this profitability is not enough to cover the average cost of funding.

## **INDUSTRY ANALYSIS**

Daktronics Inc. operates under Signs and Advertising Specialties (SIC code 3993) and NAICS code of Sign Manufacturing (339950). This industry is primarily engaged in manufacturing signs and related displays of all materials that include electrical, mechanical, cutout or plate signs and advertising displays. The sign manufacturing industry is quite old and many companies have existed for a long time. Daktronics is in maturity stage of the business life cycle. Due to rapid technological advancements over the years this industry has faced many challenges to operate in a growing digital marketplace. Rival firms compete based on different aspects however the major stand out factors has been offering high quality after sales service and prices that match industry standards.

This industry consists of major players like Daktronics Inc., Brady Corporation and LSI however; it also faces competition from electronics display divisions of major electronics manufacturers such as Samsung (South Korea) and Panasonic (Japan).

### **Threat of New Entrants**

The barrier to entry in the sign manufacturing industry is low making it easier for new players to enter the market. New entrants bring more competition that eventually forces rivals to come up with new innovation and strategies to deal with it. Daktronics is a known player in the sign manufacturing industry however it can deal with new entrants by adopting low pricing strategy, innovating new products and services by investing in research and development, building economies of scale to have cost advantage over new entrants and by finding ways to retain customers.

### **Bargaining Power of Suppliers**

There are numerous suppliers in the sign manufacturing industry making the bargaining power of suppliers low. The suppliers provide standardized products with minimal differentiation making it easier for companies to switch between suppliers. This also means that suppliers have less control over prices. Daktronics sources its raw materials from around the world and can add multiple suppliers to their supply chain based on geography and bargain for lower prices for raw materials.

### **Bargaining Power of Buyers**

Bargaining power of buyers is high in this industry. In addition to this the industry is also price sensitive as many companies in the industry offer products at competitive prices. Daktronics has large customer base that are scattered worldwide ranging from local business owners to professional sports arena operators. Two major customers account for more than 50 percent of sales and loss of one or more customers could have an unfavorable effect on Daktronics.

### **Threat of Substitutes**

The threat of substitutes is low. There are few substitute products provided by rival and small companies. However because Daktronics holds numerous patents, copyrights and trademarks on a global basis it has competitive advantage over other companies. Because of their patented technology and products buyers are less likely to switch to substitute products from other companies.

### **Rivalry Among Existing Competitors**

The sign manufacturing industry is dynamic with ongoing growing digital marketplace. This industry has high number of companies. Daktronics faces competition from companies ranging in size and product offering that are located in the United States as well as foreign countries. Hence the rivalry among existing firms is a stronger force within the industry. To remain competitive Daktronics has to respond quickly to customers' needs, enhance existing products, introduce new products and features and continue to price products competitively.

### **Industry Trends**

The sign manufacturing industry is characterized by ongoing innovations, product improvement and development. Over the years the products offered by Daktronics has significantly evolved from scoreboards and matrix displays with related software applications to complex, integrated visual display systems held together through sophisticated control systems. Companies in this industry are rapidly adopting new technological changes and investing in research and development to compete.

## **RISK ANALYSIS**

Daktronics operates in a dynamic industry that consists of various risk factors. The products offered compete with other forms of advertising such as television, print media and fixed display signs. Daktronics relies heavily on digital technologies for its daily operation and collection and retention of business data. Any disruption in the digital technologies could affect the company's business as it may face significant fines and penalties under various domestic and global laws revolving around data loss and lack of data protection. The company also has to constantly keep up with rapidly changing technology to compete effectively. In addition to this other risks such as price fluctuations or shortages of raw materials might negatively affect the company's ability to manufacture products.

The overall performance of the company also depends on economic cycles, which may affect the demand and supply of products, foreign exchange markets, credit restriction and profit. Since Daktronics operates globally it is exposed to global political, economic, and socio-cultural changes. It has to comply with rules and laws of different countries in which it is operating and any unfavorable political developments, trading policies, economic changes may pose difficulty in managing global operations. Also global tax law changes may adversely affect the company's profits as it is subject to income tax laws of United States as well as foreign countries.

Daktronics also relies on third parties for on-site installation and service related activities. There is a risk that the company may hire below par subcontractors who may fail to provide favorable services and have disputes with them. The company's business also involves use of hazardous materials and it must comply with environmental, health and safety laws and regulations which is expensive and can restrict how the company does business.

## **SHAREHOLDER ANALYSIS**

The ownership of Daktronics Inc. is divided among mutual fund holders, individual stakeholders and other institutional holders. Table 5 shows the top five mutual fund holders of Daktronics.

**Table 5: Top 5 Mutual Fund Holders**

	<b>Holder Name</b>	<b>Shares Outstanding (%)</b>	<b>Shares Held at 2/22/2019</b>	<b>Total Value (USD)</b>
1	iShares Core S&P Small Cap ETF	5.37	2,419,082	19,642,946
2	Vanguard Total Stock Market Index Fund	2.74	1,233,480	10,015,858
3	DFA U.S. Small Cap Series	2.27	1,019,651	8,279,566
4	iShares Russell 2000 ETF	1.66	745,236	6,051,316
5	iShares S&P Small Cap 600 Value ETF	1.57	705,088	5,725,315

Source: CNN Money, March 19, 2019

There are a total of 160 numbers of institutional investors and the total value of shares held among them is USD 200 million. The total shares outstanding as of March 19, 2019 were 45 million. The top five institutional holders are highlighted in Table 6.

**Table 6: Top 5 Holders of Institutional Holdings**

	<b>Holder Name</b>	<b>Shares Outstanding (%)</b>	<b>Shares Held at 2/22/2019</b>	<b>Total Value (USD)</b>
1	Blackrock Inc.	11.82	5,321,509	43,210,653
2	Dimensional Fund Advisors LP	6.92	3,114,297	25,288,092
3	Vanguard Group Inc.	6.26	2,817,580	22,878,750
4	Ceredex Value Advisors LLC	3.00	1,351,584	10,974,862
5	First Bank & Trust	2.39	1,076,620	8,742,154

Source: NASDAQ, CNN Money, March 19, 2019

Table 7 lists the insider ownership as of February 2019 with the name and total shares held as given in Daktronics' website.

**Table 7: Insider Ownership as of February 2019**

Name	Title	Total Shares Held
James B. Morgan	Director	1,373,520
Carla S. Gatzke	Secretary and VP of Human Resource	438,428
Reece A. Kurtenbach	Director, Chairman, President and CEO	285,107
Matthew John Kurtenbach	VP of Manufacturing	201,052
Bradley T. Wiemann	Exec. Vice President	95,846
Nancy D. Frame	Director	71,847
Robert G. Dutcher	Director	49,291
Byron J. Anderson	Director	40,465
Kevin P. McDermott	Director	29,272
John P. Friel	Director	24,625
Sheila Anderson	CFO and Treasurer	14,470

Source: *Daktronics Inc.*'s website

There have been 17 insider trades with 101,497 shares being traded in 2018. Out of the 17 insider trades 6 have been open market buys and 11 were insider sells. Table 8 lists the top five insider transactions of 2018 for Daktronics Inc.

**Table 8: Top 5 Insider Transactions of 2018**

	Name	Shares Traded	Transaction Type
1	James B. Morgan	10,000	Bona fide gift
2	Carla S. Gatzke	5,701	Sell
3	Carla S. Gatzke	5,411	Option Execute
4	Carla S. Gatzke	5,701	Sell
5	Sheila Anderson	3500	Option Execute

Source: *Daktronics Inc.*'s website

According to the 2018 Annual Report of Daktronics Inc., the Board of Directors approved a stock repurchase program in June 17, 2016, under which Daktronics Inc. could purchase up to USD 40 million of its outstanding stocks. There has been no repurchase of outstanding common stock during the fiscal year 2018.

## **HISTORICAL FINANCIAL ANALYSIS**

Productivity, liquidity, leverage, and profitability ratios between Daktronics and its competitor LSI Industries were carried out and there are various ratios that are worth

stating. With regards to Daktronics' productivity performance, their receivables turnover ratio for the years 2015 to 2018 has been higher than that of LSI. Daktronics had receivables turnover of 7.89 in 2018 whereas LSI had receivables turnover of 6.76 in 2018. This indicates that Daktronics can collect funds more efficiently than LSI and that the company has a high quantity of quality customers that pay their debts swiftly. In 2018, Daktronics has growth in sales of 4.1 percent compared to 3.2 percent of LSI. The total asset turnover of Daktronics is higher than LSI in 2018 and 2017, which indicates that Daktronics is using its assets efficiently to generate revenue compared to LSI. The relevant productivity ratios for Daktronics and LSI are listed in Table 9.

**Table 9: Productivity Ratio Analysis**

<b>Productivity Ratios</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
Daktronics Receivables Turnover	7.89	7.44	7.35	7.62
LSI Receivables Turnover	6.76	6.78	6.86	7.05
Daktronics Growth in Sales	4.1%	2.9%	-7.4%	N/A
LSI Growth in Sales	3.2%	2.9%	4.7%	2.8%
Daktronics Total Asset Turnover	1.70	1.65	1.63	1.62
LSI Total Asset Turnover	1.49	1.29	1.65	1.70

With regards to liquidity both companies maintain liquidity ratios similar to one another as seen in Table 10. Daktronics and LSI both have current ratio greater than one from 2014 to 2018. However the results show that Daktronics is slightly more liquid compared to LSI. The quick ratio of Daktronics for the year 2018 is 1.9 and 1.94 for year 2017. LSI's quick ratio for 2018 is 1.4 and 1.26 for the year 2017. Here the results suggest that Daktronics is quickly converting receivables into cash and is easily able to cover its financial obligations compared to LSI.

**Table 10: Liquidity Ratio Analysis**

<b>Liquidity Ratios</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
Daktronics Current Ratio	2.66	2.62	2.72	3.04
LSI Current Ratio	2.61	2.36	3.26	3.19
Daktronics Quick Ratio	1.9	1.94	1.95	2.37
LSI Quick Ratio	1.4	1.26	2.13	2.02

Daktronics has overall higher leverage ratios than LSI. The total debt-to-equity of Daktronics in 2018 is 0.82, which has slightly increased from 0.79 in 2017. The interest coverage ratio of Daktronics in 2018 is 57.42 compared to 5.82 of LSI. A low interest coverage ratio means that there is low amount of profits available to meet the interest expense on the debt. Similarly, the debt-to-asset ratios of both the companies are less than 0.5 from year 2015 to 2018. Lower the debt-to-asset ratio; the less risky is the company. This means that the company owns more assets than liabilities and can meet its obligations by selling its assets if required. Looking at Table 11, LSI's ratio is slightly lower than that of Daktronics, which hints that Daktronics is slightly more risky to invest in comparison.

**Table 11: Leverage Ratio Analysis**

<b>Leverage Ratios</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
Daktronics Total Debt to Equity	0.82	0.79	0.74	0.79
LSI Total Debt to Equity	0.65	0.60	0.26	0.26
Daktronics Interest Coverage Ratio	57.42	67.04	10.94	140.29
LSI Interest Coverage Ratio	-12.60	5.82	387.67	167.40
Daktronics Debt to Asset Ratio	0.45	0.44	0.43	0.44
LSI Debt to Asset Ratio	0.39	0.38	0.20	0.21

The profitability ratios of Daktronics are slightly better than LSI's. Daktronics' gross profit margin is 26.8 percent in 2018. Compared to LSI, Daktronics has .71 percent higher gross profit in 2018. Daktronics' NOPAT margin has been decreasing over the years, going from 1.75 percent in 2017 to 0.95 percent in 2018 whereas LSI has increased NOPAT margin from 2.3 percent in 2017 to 4.15 percent in 2018. Daktronics has seen their net margin decrease from 1.8 percent in 2017 to 0.9 percent in 2018. LSI has also seen a decrease in their net margin, going from a net margin of 0.9 percent in 2017 to -5.7 percent in 2018.



Daktronics has ROIC ratios of 0.44 percent in 2016, 5.22 percent in 2017 and 2.75 percent in 2018. LSI has ROIC ratios of 3.9 percent in 2015, 6.94 percent in 2016, 2.35 percent in 2017, and -8.94 percent in 2018. Daktronics 2018 ROIC value is higher than that of LSI, however it is below the calculated WACC of 9.61 percent, which indicates that value is not being created for Daktronics. Daktronics' ROE has remained higher than LSI's except in 2016. The ROE of Daktronics in 2018 is 6.31 percent compared to -15.55 percent of LSI in 2018. Investors prefer high ROE as it indicates that the Daktronics is using shareholders' funds effectively. Details of profitability ratios are given in Table 12.

**Table 12: Profitability Ratios**

<b>Profitability Ratios</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
Daktronics NOPAT Margin	0.8%	1.7%	0.2%	3.5%
LSI NOPAT Margin	4.1%	2.3%	0.7%	0.0%
Daktronics Net Margin	0.9%	1.8%	0.4%	3.4%
LSI Net Margin	-5.7%	0.9%	2.9%	1.7%
Daktronics ROIC Ratio	2.75%	5.22%	0.44%	N/A
LSI ROIC Ratio	-8.94%	2.35%	6.94%	3.9%
Daktronics ROE Ratio	6.31%	7.78%	1.24%	14.75%
LSI ROE Ratio	-15.55%	2.25%	8.97%	5.27%

By performing financial ratio analysis with Daktronics and LSI, it is apparent that the Daktronics is doing slightly well in many categories.

## **PROSPECTIVE FINANCIAL ANALYSIS**

Daktronics reported its third quarter fiscal year 2019 results on February 20, 2019. Net sales, operating income, net income, and earnings per share as of January 26, 2019, were USD 441.9 million, USD 5.5 million, USD 9.9 million, and USD 0.22 per diluted share, respectively. Daktronics has a tax benefit of USD 4.1 million for the third quarter of fiscal 2019 which is the result of the release of USD 2.8 million in unrecognized tax benefits related to a lapse of statute and the release of USD 0.5 million for a valuation allowance reversal related to foreign net operating loss carry forwards. During the third quarter of fiscal 2018, the company accounted for the revaluation of deferred tax benefits due to the enactment of new U.S. tax laws creating a charge of USD 3.7 million.

Reece Kurtenbach, Chairman, President, has recently stated that the sales and profits are historically lower because of the seasonality of sports business, construction cycles, current global tariff and trade environment in addition to USD 1.8 million expenses for discrete project and litigation claims. However its order booking remains strong and the long-term outlook of the company seems optimistic.

By analyzing historical data and evaluating historical ratios about the company, I projected pro-forma financial statements for Daktronics. I estimate that over the next five years Daktronics will have increase in operating income as sales are expected to increase over the years. Daktronics' estimated price for the closing date of March 29, 2019 is USD 5.78, which is below market close price of USD 7.45 on March 29, 2019 with a difference of USD 1.67.

I estimate the price to be USD 5.78 at the end of fiscal year 2019. My estimated WACC for Daktronics is 9.61 percent. Daktronics' net income is forecasted to increase from 2020 onwards. The net income for the year 2019 is low because of construction cycles, current global tariff and trade environment. In addition the company had to use USD 1.8 million for litigation claims.

## **VALUATION AND INVESTMENT DECISION**

I used valuation model that discounts free cash flows at the Weighted Average Cost of Capital (WACC). I used SEC EDGAR system to download financial statements for the latest five-year period. The most recent audited information for Daktronics is January 26, 2019. The cost of equity is calculated using the Capital Asset Pricing Model assuming a market risk premium of 8.5 percent, a beta of .90, and a risk free rate of 3 percent. I estimated the cost of long- term and short-term debt before taxes to be 4.93 percent and 5 percent, respectively, and a tax rate of 21 percent.

Using this information along with market weights to estimate the proportion of debt and equity, I obtained a WACC of 9.61 percent with price per share USD 5.78 as of March 29, 2019 and expected to remain at USD 5.78 at the fiscal year end. The stock price of Daktronics at market close on March 29, 2019, was USD 7.45, which is higher than the calculated intrinsic value. This indicates that Daktronics' shares are trading at a slightly higher value at the stock market.

I would give an investment rating of hold for Daktronics as the stock is expected perform at the same rate as other stocks in the sector. This rating conveys that investors with existing long positions should not sell and investors without a position should not purchase. In my opinion investors holding Daktronics' stock for a long period of time can profit from quarterly dividends and potential price increase over time.

## **SOURCES OF INFORMATION**

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**Daktronics Inc. (NASDAQ: DAKT)**

*In thousands of USD*

**Income Statement**

	4/30/2017	4/30/2018	4/30/2019	4/30/2020	4/30/2021	4/30/2022	4/30/2023	4/30/2024
Sales	\$ 586,539	\$ 610,530	\$ 589,265	\$ 654,085	\$ 706,411	\$ 755,860	\$ 808,770	\$ 857,296
Costs of goods sold (COGS)	\$ 427,562	\$ 447,077	\$ 434,047	\$ 481,793	\$ 520,336	\$ 556,759	\$ 595,733	\$ 631,477
Sales, general and administrative expense (SGA)	\$ 124,994	\$ 133,209	\$ 133,781	\$ 137,375	\$ 148,365	\$ 158,751	\$ 169,863	\$ 180,055
Depreciation	\$ 18,562	\$ 17,784	\$ 14,054	\$ 18,203	\$ 19,660	\$ 21,036	\$ 22,508	\$ 23,859
<b>Operating profit</b>	<b>\$ 15,421</b>	<b>\$ 12,460</b>	<b>\$ 7,383</b>	<b>\$ 16,714</b>	<b>\$ 18,051</b>	<b>\$ 19,314</b>	<b>\$ 20,666</b>	<b>\$ 21,906</b>
Interest expense	-\$ 230	-\$ 217	-\$ 115	\$ 859	\$ 1,939	\$ 2,137	\$ 2,337	\$ 2,556
Interest income	\$ 751	\$ 723	\$ 951	\$ 892	\$ 682	\$ 563	\$ 455	\$ 334
Non operating income (Expense)	-\$ 354	-\$ 537	-\$ 564	-\$ 626	-\$ 676	-\$ 723	-\$ 774	-\$ 821
Earnings before taxes (EBT)	\$ 15,588	\$ 12,429	\$ 7,655	\$ 16,120	\$ 16,117	\$ 7,675	\$ 7,927	\$ 7,558
Tax expense	\$ 5,246	\$ 6,867	-\$ 5,493	\$ 3,385	\$ 3,385	\$ 3,574	\$ 3,782	\$ 3,961
Net income before extraordinary items	\$ 10,342	\$ 5,562	\$ 13,148	\$ 12,735	\$ 12,732	\$ 13,443	\$ 14,228	\$ 14,902
After-tax extraordinary income (Expense)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Net income (NI)</b>	<b>\$ 10,342</b>	<b>\$ 5,562</b>	<b>\$ 13,148</b>	<b>\$ 12,735</b>	<b>\$ 12,732</b>	<b>\$ 13,443</b>	<b>\$ 14,228</b>	<b>\$ 14,902</b>
Dividends-- preferred	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Dividends-- common	\$ 13,651	\$ 12,424	\$ 9,403	\$ 9,403	\$ 10,343	\$ 11,378	\$ 12,515	\$ 13,517
Additions to RE	-\$ 3,309	-\$ 6,862	\$ 3,745	\$ 3,332	\$ 2,389	\$ 2,066	\$ 1,713	\$ 1,385

**Balance Sheet**

	4/30/2017	4/30/2018	4/30/2019	4/30/2020	4/30/2021	4/30/2022	4/30/2023	4/30/2024
<b>Assets</b>								
Cash	\$ 32,623	\$ 29,727	\$ 33,281	\$ 25,171	\$ 27,185	\$ 29,088	\$ 31,124	\$ 32,991
Inventory	\$ 66,486	\$ 75,335	\$ 72,187	\$ 78,777	\$ 85,079	\$ 91,035	\$ 97,407	\$ 103,252
Accounts receivable	\$ 78,846	\$ 77,387	\$ 77,743	\$ 86,392	\$ 93,304	\$ 99,835	\$ 106,823	\$ 113,233
Other short-term operating assets	\$ 10,438	\$ 16,166	\$ 15,336	\$ 17,209	\$ 18,585	\$ 19,886	\$ 21,278	\$ 22,555

Short-term investments	\$ 69,332	\$ 65,518	\$ 66,057	\$ 50,498	\$ 41,207	\$ 32,784	\$ 23,298	\$ 14,853
Total current assets	\$ 257,725	\$ 264,133	\$ 264,604	\$ 258,047	\$ 265,359	\$ 272,627	\$ 279,931	\$ 286,883
Net plant, property, & equipment (PPE)	\$ 66,749	\$ 68,059	\$ 65,765	\$ 76,327	\$ 82,433	\$ 88,204	\$ 94,378	\$ 100,040
Other long-term operating assets	\$ 12,517	\$ 11,946	\$ 13,397	\$ 13,465	\$ 14,543	\$ 15,561	\$ 16,650	\$ 17,649
Long-term investments	\$ 18,442	\$ 14,662	\$ 14,986	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Total assets</b>	<b>\$ 355,433</b>	<b>\$ 358,800</b>	<b>\$ 358,752</b>	<b>\$ 347,839</b>	<b>\$ 362,335</b>	<b>\$ 376,391</b>	<b>\$ 390,958</b>	<b>\$ 404,572</b>
<b>Liabilities and Equity</b>								
Accounts payable (AP)	\$ 51,499	\$ 48,845	\$ 35,117	\$ 50,917	\$ 54,991	\$ 58,840	\$ 62,959	\$ 66,736
Accruals	\$ 45,589	\$ 49,471	\$ 53,775	\$ 52,278	\$ 56,460	\$ 60,412	\$ 64,641	\$ 68,520
Other operating current liabilities	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
All short-term debt	\$ 1,409	\$ 1,088	\$ 1,199	\$ -	\$ -	\$ -	\$ -	\$ -
Total current liabilities	\$ 98,497	\$ 99,404	\$ 90,091	\$ 103,195	\$ 111,451	\$ 119,253	\$ 127,600	\$ 135,256
Long-term debt	\$ 17,434	\$ 19,502	\$ 16,213	\$ 39,339	\$ 43,345	\$ 47,400	\$ 51,851	\$ 56,372
Deferred taxes	\$ 836	\$ 614	\$ 597	\$ 822	\$ 667	\$ 801	\$ 857	\$ 908
Preferred stock	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Other long-term liabilities	\$ 40,380	\$ 41,664	\$ 50,700	\$ -	\$ -	\$ -	\$ -	\$ -
Total liabilities	\$ 157,147	\$ 161,184	\$ 157,601	\$ 143,356	\$ 155,463	\$ 167,454	\$ 180,308	\$ 192,536
Par plus PIC Less treasury (and other adjustments)	\$ 213,585	\$ 219,777	\$ 219,567	\$ 219,567	\$ 219,567	\$ 219,567	\$ 219,567	\$ 219,567
Retained earnings (RE)	-\$ 15,299	-\$ 22,161	-\$ 18,416	\$ 15,084	\$ 12,695	-\$ 10,629	-\$ 8,917	-\$ 7,531
Total common equity	\$ 198,286	\$ 197,616	\$ 201,151	\$ 204,483	\$ 206,872	\$ 208,938	\$ 210,650	\$ 212,036
<b>Total liabilities and equity</b>	<b>\$ 355,433</b>	<b>\$ 358,800</b>	<b>\$ 358,752</b>	<b>\$ 347,839</b>	<b>\$ 362,335</b>	<b>\$ 376,391</b>	<b>\$ 390,958</b>	<b>\$ 404,572</b>

<b>Statement of Cash Flows</b>	<b>4/30/2017</b>	<b>4/30/2018</b>	<b>4/30/2019</b>	<b>4/30/2020</b>	<b>4/30/2021</b>	<b>4/30/2022</b>	<b>4/30/2023</b>	<b>4/30/2024</b>
<b>Operating Activities</b>								
Net income	\$ 10,342	\$ 5,562	\$ 13,148	\$ 12,735	\$ 12,732	\$ 13,443	\$ 14,228	\$ 14,902
Depreciation	\$ 18,562	\$ 17,784	\$ 14,054	\$ 18,203	\$ 19,660	\$ 21,036	\$ 22,508	\$ 23,859
Change in deferred tax	\$ 82	-\$ 222	-\$ 17	\$ 225	-\$ 155	\$ 134	\$ 56	\$ 51
Change in inventory	\$ 3,341	-\$ 8,849	\$ 3,148	-\$ 6,590	-\$ 6,302	-\$ 5,956	-\$ 6,372	-\$ 5,844
Change in accounts receivable	-\$ 1,292	\$ 1,459	-\$ 356	-\$ 8,649	-\$ 6,911	-\$ 6,531	-\$ 6,988	-\$ 6,409
Change in other short-term operating assets	\$ 4,014	-\$ 5,728	\$ 830	-\$ 1,873	-\$ 1,377	-\$ 1,301	-\$ 1,392	-\$ 1,277
Change in accounts payable	\$ 8,058	-\$ 2,654	-\$ 13,728	\$ 15,800	\$ 4,073	\$ 3,849	\$ 4,119	\$ 3,778
Change in accruals	-\$ 420	\$ 3,882	\$ 4,304	-\$ 1,497	\$ 4,182	\$ 3,952	\$ 4,229	\$ 3,878
Change in other current liabilities	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Net cash from operating activities</b>	<b>\$ 42,687</b>	<b>\$ 11,234</b>	<b>\$ 21,383</b>	<b>\$ 28,355</b>	<b>\$ 25,903</b>	<b>\$ 28,626</b>	<b>\$ 30,387</b>	<b>\$ 32,938</b>
<b>Investing Activities</b>								
Investment in PPE	-\$ 12,148	-\$ 19,094	-\$ 11,760	-\$ 28,765	-\$ 25,766	-\$ 26,806	-\$ 28,682	-\$ 29,521
Investment in other long-term oper. ass.	\$ 3,320	\$ 571	-\$ 1,451	-\$ 68	-\$ 1,077	-\$ 1,018	-\$ 1,089	-\$ 999
<b>Net cash from investing activities</b>	<b>-\$ 8,828</b>	<b>-\$ 18,523</b>	<b>-\$ 13,211</b>	<b>-\$ 28,834</b>	<b>-\$ 26,843</b>	<b>-\$ 27,824</b>	<b>-\$ 29,772</b>	<b>-\$ 30,520</b>
<b>Financing Activities</b>								
Change in short-term investments	-\$ 14,262	\$ 3,814	-\$ 539	\$ 15,559	\$ 9,291	\$ 8,423	\$ 9,485	\$ 8,446
Change in long-term investments	-\$ 2,725	\$ 3,780	-\$ 324	\$ 14,986	\$ -	\$ -	\$ -	\$ -
Change in short-term debt	\$ 824	-\$ 321	\$ 111	-\$ 1,199	\$ -	\$ -	\$ -	\$ -
Change in long-term debt	\$ 486	\$ 2,068	-\$ 3,289	\$ 23,126	\$ 4,006	\$ 4,055	\$ 4,451	\$ 4,521
Preferred dividends	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Change in preferred stock	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Change in other long-term liabilities	-\$ 764	\$ 1,284	\$ 9,036	-\$ 50,700	\$ -	\$ -	\$ -	\$ -
Change in common stock (Par + PIC)	\$ 528	\$ 6,192	-\$ 210	\$ -	\$ -	\$ -	\$ -	\$ -
Common dividends	-\$ 13,651	-\$ 12,424	-\$ 9,403	-\$ 9,403	-\$ 10,343	-\$ 11,378	-\$ 12,515	-\$ 13,517
<b>Net cash from financing activities</b>	<b>-\$ 29,564</b>	<b>\$ 4,393</b>	<b>-\$ 4,618</b>	<b>-\$ 7,631</b>	<b>\$ 2,954</b>	<b>\$ 1,101</b>	<b>\$ 1,420</b>	<b>-\$ 550</b>
Net cash flow	\$ 4,295	-\$ 2,896	\$ 3,554	-\$ 8,110	\$ 2,014	\$ 1,903	\$ 2,036	\$ 1,867
Starting cash	\$ 28,328	\$ 32,623	\$ 29,727	\$ 33,281	\$ 25,171	\$ 27,185	\$ 29,088	\$ 31,124
<b>Ending cash</b>	<b>\$ 32,623</b>	<b>\$ 29,727</b>	<b>\$ 33,281</b>	<b>\$ 25,171</b>	<b>\$ 27,185</b>	<b>\$ 29,088</b>	<b>\$ 31,124</b>	<b>\$ 32,991</b>

<b>Ratios</b>	<b>2019</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
<b><i>Productivity Ratios</i></b>					
Growth in sales	-3.5%	4.1%	2.9%	-7.4%	N/A
Receivables turnover	7.58	7.89	7.44	7.35	7.62
Inventory turnover	8.16	8.10	8.82	8.17	9.57
Operating working capital turnover	5.37	6.09	6.42	5.66	4.76
Net fixed asset turnover	7.44	7.63	7.40	6.41	7.71
Total asset turnover	1.64	1.70	1.65	1.63	1.62
Invested capital turnover	3.12	3.39	3.44	3.01	2.94
<b><i>Liquidity Ratios</i></b>					
Current ratio	2.94	2.66	2.62	2.72	3.04
Quick ratio	2.14	1.90	1.94	1.95	2.37
Cash ratio	1.10	0.96	1.04	0.93	1.29
Short-term investments over invested capital	0.35	0.36	0.41	0.29	0.32
Operating Cycle	92.87	91.30	90.44	94.35	86.07
Cash Cycle	71.12	62.10	58.39	66.54	54.81
<b><i>Financial Risk (Leverage) Ratios</i></b>					
Total debt-to-equity ratio	0.78	0.82	0.79	0.74	0.79
Total debt-to-equity ratio (excluding deferred taxes)	0.78	0.81	0.79	0.74	0.79
Total financial debt-to-equity ratio	0.09	0.10	0.10	0.09	0.08
Interest coverage ratio (accounting-based)	-64.38	-57.42	-67.05	-10.94	-140.29
Interest coverage ratio (cash-based)	-186.95	-139.37	-147.75	-85.25	-208.17
Total debt-to-assets ratio	0.44	0.45	0.44	0.43	0.44
Total financial debt over invested capital	0.05	0.06	0.05	0.05	0.05
Long-term financial debt over invested capital	0.09	0.11	0.10	0.09	0.08
<b><i>Profitability/Valuation Ratios</i></b>					
Gross profit margin	26.3%	26.8%	27.1%	24.2%	25.9%
EBITDA margin	3.6%	5.0%	5.8%	3.4%	7.5%
Operating profit margin	1.3%	2.0%	2.6%	0.4%	5.1%

NOPAT margin	2.4%	0.8%	1.7%	0.2%	3.4%
Earnings before taxes margin	1.3%	2.0%	2.7%	0.5%	5.1%
Net margin	2.2%	0.9%	1.8%	0.4%	3.4%
Return on Assets	2.06%	3.47%	4.34%	0.71%	8.24%
Net investment rate	61.18%	207.16%	-193.42%	-2153.28%	1002.81%
Dividend payout ratio	71.52%	223.37%	132.00%	851.82%	83.22%
ROIC	7.72%	2.75%	5.22%	0.44%	N/A
ROE	3.67%	6.31%	7.78%	1.24%	14.75%