

LSI INDUSTRIES INC  
Form 10-Q  
November 07, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

X QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2018.

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_.

Commission File No. 0-13375

LSI Industries Inc.

State of Incorporation - Ohio      IRS Employer I.D. No. 31-0888951

10000 Alliance Road

Cincinnati, Ohio 45242

(513) 793-3200

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Indicate by checkmark 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 checkmark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

YES  NO

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

Large accelerated filer [  ]      Accelerated filer [  ]  
Non-accelerated filer [  ]      Smaller reporting company [  ]  
Emerging growth company [  ]

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

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

As of October 25, 2018 there were 26,025,256 shares of the registrant's common stock, no par value per share, outstanding.

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LSI INDUSTRIES INC.

FORM 10-Q

FOR THE QUARTER ENDED SEPTEMBER 30, 2018

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***“Safe Harbor” Statement under the Private Securities Litigation Reform Act of 1995***

*This Form 10-Q contains certain forward-looking statements that are subject to numerous assumptions, risks or uncertainties. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. Forward-looking statements may be identified by words such as “estimates,” “anticipates,” “projects,” “plans,” “expects,” “intends,” “believes,” “seeks,” “may,” “will,” “should” or the negative versions of those words and similar expressions, and by the context in which they are used. Such statements, whether expressed or implied,*

*are based upon current expectations of the Company and speak only as of the date made. Actual results could differ materially from those contained in or implied by such forward-looking statements as a result of a variety of risks and uncertainties over which the Company may have no control. These risks and uncertainties include, but are not limited to, the impact of competitive products and services, product demand and market acceptance risks, potential costs associated with litigation and regulatory compliance, reliance on key customers, financial difficulties experienced by customers, the cyclical and seasonal nature of our business, the adequacy of reserves and allowances for doubtful accounts, fluctuations in operating results or costs whether as a result of uncertainties inherent in tax and accounting matters or otherwise, unexpected difficulties in integrating acquired businesses, the ability to retain key employees of acquired businesses, unfavorable economic and market conditions, the results of asset impairment assessments and the other risk factors that are identified herein. You are cautioned to not place undue reliance on these forward-looking statements. In addition to the factors described in this paragraph, the risk factors identified in our Form 10-K and other filings the Company may make with the SEC constitute risks and uncertainties that may affect the financial performance of the Company and are incorporated herein by reference. The Company does not undertake and hereby disclaims any duty to update any forward-looking statements to reflect subsequent events or circumstances.*

**PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS**

LSI INDUSTRIES INC.

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended September 30	
	2018	2017
<i>(In thousands, except per share data)</i>		
Net sales	\$84,957	\$87,466
Cost of products and services sold	63,541	63,763
Restructuring costs	155	--
Gross profit	21,261	23,703
Selling and administrative expenses	18,327	20,517
Impairment of goodwill	--	28,000
Operating income (loss)	2,934	(24,814)
Interest (income)	(14 )	(8 )
Interest expense	532	411
Income (loss) before income taxes	2,416	(25,217)
Income tax expense (benefit)	667	(9,588 )

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Net income (loss)	\$1,749	\$(15,629)
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Earnings (Loss) per common share (see Note 4)

Basic	\$0.07	\$(0.61 )
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Diluted	\$0.07	\$(0.61 )
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Weighted average common shares outstanding

Basic	26,032	25,791
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Diluted	26,365	25,791
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The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

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## LSI INDUSTRIES INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

<i>(In thousands, except shares)</i>	September 30, 2018	June 30, 2018
<b>ASSETS</b>		
Current Assets		
Cash and cash equivalents	\$ 4,162	\$ 3,178
Accounts receivable, less allowance for doubtful accounts of \$363 and \$409, respectively	59,781	50,609
Inventories	49,580	50,994
Refundable income taxes	1,197	1,784
Other current assets	3,625	3,516
Total current assets	118,345	110,081
Property, Plant and Equipment, at cost		
Land	6,718	6,470
Buildings	35,984	35,961
Machinery and equipment	77,658	77,108
Construction in progress	1,261	1,340
	121,621	120,879
Less accumulated depreciation	(79,098 )	(77,176 )
Net property, plant and equipment	42,523	43,703
Goodwill	30,538	30,538
Other Intangible Assets, net	34,718	35,409
Other Long-Term Assets, net	9,420	9,786

Total assets	\$ 235,544	\$ 229,517
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The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.



LSI INDUSTRIES INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

<i>(In thousands, except shares)</i>	September 30, 2018	June 30, 2018
<b>LIABILITIES &amp; SHAREHOLDERS' EQUITY</b>		
Current Liabilities		
Accounts payable	\$ 23,774	\$ 17,927
Accrued expenses	21,949	24,272
Total current liabilities	45,723	42,199
Long-Term Debt	46,152	45,360
Other Long-Term Liabilities	2,606	2,707
Commitments and Contingencies (Note 12)		
Shareholders' Equity		
Preferred shares, without par value; Authorized 1,000,000 shares, none issued	--	--
Common shares, without par value; Authorized 40,000,000 shares; Outstanding 25,799,257 and 25,641,913 shares, respectively	124,871	124,104
Treasury shares, without par value;	(1,845 )	(2,110 )
Deferred compensation plan	1,869	2,133
Retained earnings	16,168	15,124
Total shareholders' equity	141,063	139,251
Total liabilities & shareholders' equity	\$ 235,544	\$ 229,517

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.



LSI INDUSTRIES INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

<i>(In thousands)</i>	Three Months Ended September 30	
	2018	2017
<b>Cash Flows from Operating Activities</b>		
Net income (loss)	\$1,749	\$(15,629)
Non-cash items included in net income:		
Depreciation and amortization	2,643	2,572
Deferred income taxes	85	(10,815)
Impairment of goodwill	--	28,000
Deferred compensation plan	127	160
Stock compensation expense	551	984
Issuance of common shares as compensation	90	78
Loss on disposition of fixed assets	--	(31 )
Allowance for doubtful accounts	(19 )	49
Inventory obsolescence reserve	766	143
<b>Changes in certain assets and liabilities</b>		
Accounts receivable	(4,218 )	(5,421 )
Inventories	(3,519 )	683
Refundable income taxes	587	775
Accounts payable	5,723	(1,559 )
Accrued expenses and other	(3,172 )	(3,133 )
Customer prepayments	795	419
Net cash flows provided by (used in) operating activities	2,188	(2,725 )
<b>Cash Flows from Investing Activities</b>		
Proceeds from the sale of assets	--	1,527
Purchases of property, plant and equipment	(648 )	(498 )
Net cash flows (used in) provided by investing activities	(648 )	1,029
<b>Cash Flows from Financing Activities</b>		
Payments of long-term debt	(23,039)	(22,247)
Borrowings of long-term debt	23,831	24,411
Cash dividends paid	(1,296 )	(1,286 )

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Shares withheld for employees taxes	(52 )	(110 )
Purchase of treasury shares	--	(106 )
Exercise of stock options	--	115
Net cash flows (used in) provided by financing activities	(556 )	777
Increase (Decrease) in cash and cash equivalents	984	(919 )
Cash and cash equivalents at beginning of period	3,178	3,039
Cash and cash equivalents at end of period	\$4,162	\$2,120

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

LSI INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

**NOTE 1 - INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

The interim condensed consolidated financial statements are unaudited and are prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information, and rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the interim financial statements include all normal adjustments and disclosures necessary to present fairly the Company's financial position as of *September 30, 2018*, the results of its operations for the *three* month periods ended *September 30, 2018* and *2017*, and its cash flows for the *three* month periods ended *September 30, 2018* and *2017*. These statements should be read in conjunction with the financial statements and footnotes included in the fiscal 2018 Annual Report on Form 10-K. Financial information as of *June 30, 2018* has been derived from the Company's audited consolidated financial statements.

**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

A summary of the Company's significant accounting policies is included in Note 1 to the audited consolidated financial statements of the Company's fiscal 2018 Annual Report on Form 10-K. Significant changes to our accounting policies as a result of adopting ASU-2014-09 "Revenue from Contracts with Customers" (Topic 606) are discussed below.

**Revenue Recognition:**

The Company recognizes revenue when it satisfies the performance obligation in its customer contracts or purchase orders. Most of the Company's products have a single performance obligation which is satisfied at a point in time when control is transferred to the customer. Control is generally transferred at time of shipment when title and risk of

ownership passes to the customer. For customer contracts with multiple performance obligations, the Company allocates the transaction price and any discounts to each performance obligation based on relative standalone selling prices. Payment terms are typically within 30 to 90 days from the shipping date, depending on our terms with the customer. The Company offers standard warranties that do *not* represent separate performance obligations.

Installation is a separate performance obligation, except for our digital signage products. For digital signage products, installation is not a separate performance obligation as the product and installation is the combined item promised in digital signage contracts. The Company is not always responsible for installation of products it sells and has no post-installation responsibilities other than standard warranties.

A number of the Company's products are highly customized. As a result, these customized products do not have an alternative use. For these products, the Company has a legal right to payment for performance to date and generally does not accept returns on these items. The measurement of performance is based upon cost plus a reasonable profit margin for work completed. Because there is no alternative use and there is a legal right to payment, the Company transfers control of the item as the item is being produced and therefore, recognizes revenue over time. The customized product types are as follows:

- Customer specific printed graphic branding
- Electrical components based on customer specifications
- Digital signage and related media content

The Company also offers installation services. Installation revenue is recognized over time as our customer simultaneously receives and consumes the benefits provided through the installation process.

For these customized products and installation services, revenue is recognized using a cost-based input method: recognizing revenue and gross profit as work is performed based on the relationship between the actual cost incurred and the total estimated cost for the contract.

Disaggregation of Revenue

The Company disaggregates the revenue from contracts with customers by the timing of revenue recognition because we believe it best depicts the nature, amount, and timing of our revenue and cash flows. The table presents a reconciliation of the disaggregation by reportable segments.

	<b>Three Months Ended September 30</b>	
	<b>Lighting Segment</b>	<b>Graphics Segment</b>
<b>Timing of revenue recognition</b>		
Products and services transferred at a point in time	\$54,249	\$ 17,694
Products and services transferred over time	7,183	5,831
	\$61,432	\$ 23,525

	<b>Three Months Ended September 30</b>	
	<b>Lighting Segment</b>	<b>Graphics Segment</b>
<b>Type of Product and Services</b>		
New Technology Products	\$51,305	\$ 2,402
Legacy Products	9,076	15,964
Turnkey Services and Other	1,051	5,159
	\$61,432	\$ 23,525

New technology products include LED lighting and controls, electronic circuit boards, and digital signage solutions. Legacy products include lighting fixtures utilizing light sources other than LED technology and printed two and three dimensional graphic products. Turnkey services and other includes installation services along with shipping and handling charges.

Practical Expedients and Exemptions

The Company's contracts with customers have an expected duration of *one* year or less, as such we apply the practical expedient to expense sales commissions as incurred, and have omitted disclosures on the amount of remaining performance obligations.

Shipping costs that are *not* material in context of the delivery of products are expensed as incurred.

The Company's accounts receivable balance represents the Company's unconditional right to receive consideration from its customers with contracts. Payments are due within *30* to *90* days of completion of the performance obligation and invoicing, therefore, does *not* contain significant financing components.

The Company collects sales tax and other taxes concurrent with revenue-producing activities and are excluded from revenue. Shipping and handling costs are treated as fulfillment activities and included in cost of products and services sold on the Consolidated Statements of Operations.

### New Accounting Pronouncements:

On *July 1, 2018*, the Company adopted ASU 2014-09. "Revenue from Contracts with Customers," (Topic 606) using the modified retrospective adoption method which requires a cumulative effect adjustment to the opening balance of retained earnings. This approach was applied to contracts that were *not* completed as of *June 30, 2018*. Results for reporting periods beginning *July 1, 2018* are presented under Topic 606, while prior period amounts are *not* adjusted and continue to be reported under the accounting standards in effect for the prior period. The Company recorded a net increase to beginning retained earnings of \$591,000 on *July 1, 2018* due to the cumulative impact of adopting Topic 606, as described below.

	Balance as of	Adjustments	Opening Balance as of
	June 30, 2018		July 1, 2018
Assets:			
Accounts receivable, net	50,609	4,935	55,544
Inventories, net	50,994	(4,167)	46,827
Other long-term assets, net	9,786	(177)	9,609
Stockholders' Equity:			
Retained earnings	15,124	591	15,715

In *February 2016*, the Financial Accounting Standards Board issued ASU 2016-02, "Leases." The amended guidance requires an entity to recognize assets and liabilities that arise from leases. The amended guidance is effective for financial statements issued for fiscal years and interim periods within those years, beginning after *December 15, 2018*, or the Company's fiscal year 2020, with early adoption permitted. The Company is currently evaluating the impact the amended guidance will have on its financial statements.

### Subsequent Events:

The Company has evaluated subsequent events for potential recognition and disclosure through the date the consolidated financial statements were filed. *No* items were identified during this evaluation that required adjustment to or disclosure in the accompanying financial statements other than noted below.



On *October 29, 2018*, The Company announced that it will permanently close its New Windsor, New York manufacturing facility. The facility manufactures indoor lighting products and is included in the results of the Lighting Segment. Production will be transferred to the Company's Erlanger, Kentucky and Blue Ash, Ohio facilities, also included in the Lighting Segment. The New Windsor facility has a workforce of *140* employees.

On October 15, 2018, the Board of Directors of the Company appointed James A. Clark as the Company's Chief Executive Officer and President. Mr. Clark entered into an Employment Agreement as of October 16, 2018 which provides that his employment with the Company shall begin on November 1, 2018. The Employment Agreement also defines his compensation and benefit package.

**Reclassifications:**

Certain prior year amounts have been reclassified to conform to the current year presentation within the cash flows from operating activities section and cash flows from financing activities section of the statement of cash flows. These reclassifications have *no* impact on net income or earnings per share.

**NOTE 3 - SEGMENT REPORTING INFORMATION**

The accounting guidance on Segment Reporting establishes standards for reporting information regarding operating segments in annual financial statements and requires selected information of those segments to be presented in financial statements. Operating segments are identified as components of an enterprise for which separate discrete financial information is available for evaluation by the chief operating decision maker (the Company's Chief Executive Officer or "CODM") in making decisions on how to allocate resources and assess performance. The Company's two operating segments are Lighting and Graphics, with one executive team under the new organizational structure reporting directly to the CODM with responsibilities for managing each segment. Corporate and Eliminations, which captures the Company's corporate administrative activities, is also reported in the segment information.

The Lighting Segment includes outdoor and indoor lighting utilizing both traditional and LED light sources that have been fabricated and assembled for the Company's markets, primarily petroleum / convenience stores, automotive dealerships, quick-service restaurants, grocery and pharmacy store, and retail/national accounts. The Company also addresses lighting product customers through the commercial industrial, stock and flow, and renovation channels. The Lighting Segment also includes the design, engineering, and manufacturing of electronic circuit boards, assemblies and sub-assemblies used to manufacture certain LED light fixtures and sold directly to customers.

Segment also includes the design, engineering, and manufacturing of electronic circuit boards, assemblies and sub-assemblies used to manufacture certain LED light fixtures and sold directly to customers.

The Graphics Segment designs, manufactures and installs exterior and interior visual image elements such as traditional graphics, interior branding, electrical and architectural signage, active digital signage along with the management of media content related to digital signage, LED video screens, and menu board systems that are either digital or traditional by design. These products are used in visual image programs in several markets including, but *not* limited to the petroleum / convenience store market, multi-site retail operations, banking, and restaurants. The Graphics Segment implements, installs and provides program management services related to products sold by the Graphics Segment and by the Lighting Segment.

The Company's corporate administration activities are reported in the Corporate and Eliminations line item. These activities primarily include intercompany profit in inventory eliminations, expense related to certain corporate officers and support staff, the Company's internal audit staff, expense related to the Company's Board of Directors, equity compensation expense for various equity awards granted to corporate administration employees, certain consulting expenses, investor relations activities, and a portion of the Company's legal, auditing and professional fee expenses. Corporate identifiable assets primarily consist of cash, invested cash (if any), refundable income taxes (if any), and deferred income taxes.

There was *no* concentration of consolidated net sales in the *three* months ended *September 30, 2018* or *2017*. There was *no* concentration of accounts receivable at *September 30, 2018* or *June 30, 2018*.

Summarized financial information for the Company's operating segments is provided for the indicated periods and as of *September 30, 2018* and *September 30, 2017*:

<i>(In thousands)</i>	Three Months Ended	
	September 30 2018	2017
<b>Net Sales:</b>		
Lighting Segment	\$61,432	\$68,428
Graphics Segment	23,525	19,038
	\$84,957	\$87,466
<b>Operating Income (Loss):</b>		
Lighting Segment	\$3,850	\$(22,930)
Graphics Segment	2,387	1,476
Corporate and Eliminations	(3,303)	(3,360)
	\$2,934	\$(24,814)
<b>Capital Expenditures:</b>		
Lighting Segment	\$276	\$261
Graphics Segment	266	182
Corporate and Eliminations	106	55
	\$648	\$498
<b>Depreciation and Amortization:</b>		
Lighting Segment	\$1,990	\$1,901
Graphics Segment	395	379
Corporate and Eliminations	258	292
	\$2643	\$2,572

	September 30, 2018	June 30, 2018
<b>Identifiable Assets:</b>		
Lighting Segment	\$ 173,254	\$ 172,799
Graphics Segment	45,493	39,881
Corporate and Eliminations	16,797	16,837
	\$ 235,544	\$ 229,517

The segment net sales reported above represent sales to external customers. Segment operating income, which is used in management's evaluation of segment performance, represents net sales less all operating expenses. Identifiable assets are those assets used by each segment in its operations.

The Company records a 10% mark-up on intersegment revenues. Any intersegment profit in inventory is eliminated in consolidation. Intersegment revenues were eliminated in consolidation as follows:

	Three Months Ended September 30	
<i>(In thousands)</i>	2018	2017
Lighting Segment inter-segment net sales	\$409	\$715
Graphics Segment inter-segment net sales	\$31	\$31

The Company's operations are located solely within the United States. As a result, the geographic distribution of the Company's net sales and long-lived assets originate within the United States.

**NOTE 4 - EARNINGS PER COMMON SHARE**

The following table presents the amounts used to compute basic and diluted earnings per common share, as well as the effect of dilutive potential common shares on weighted average shares outstanding (in thousands, except per share data):

	Three Months Ended September 30	
	2018	2017
<b><u>BASIC EARNINGS (LOSS) PER SHARE</u></b>		
Net income (loss)	\$1,749	\$(15,629)
Weighted average shares outstanding, net of treasury shares (a)	25,752	25,505
Weighted average vested restricted stock units outstanding	53	41
Weighted average shares outstanding in the Deferred Compensation Plan	227	245
Weighted average shares outstanding	26,032	25,791
Basic earnings (loss) per share	\$0.07	\$(0.61 )
<b><u>DILUTED EARNINGS (LOSS) PER SHARE</u></b>		
Net income (loss)	\$1,749	\$(15,629)
Weighted average shares outstanding		
Basic	26,032	25,791
Effect of dilutive securities (b):		
Impact of common shares to be issued under stock option plans, and contingently issuable shares, if any	333	--
Weighted average shares outstanding (c)	26,365	25,791
Diluted earnings (loss) per share	\$0.07	\$(0.61 )

(a) Includes shares accounted for like treasury stock.

- (b) Calculated using the “Treasury Stock” method as if dilutive securities were exercised and the funds were used to purchase common shares at the average market price during the period.

Options to purchase 3,146,466 common shares and 3,791,936 common shares at *September 30, 2018* and *2017*, respectively, were *not* included in the computation of the *three* month period for diluted earnings (loss) per share, (c) respectively, because the exercise price was greater than the average fair market value of the common shares. For the *three* months ended *September 30, 2017*, the effect of dilutive securities was *not* included in the calculation of diluted earnings (loss) per share because there was a net operating loss for the period.

**NOTE 5 - INVENTORIES**

The following information is provided as of the dates indicated:

<i>(In thousands)</i>	September 30, 2018	June 30, 2018
Inventories:		
Raw materials	\$ 33,131	\$ 31,795
Work-in-process	1,937	3,833
Finished goods	14,512	15,366
Total Inventories	\$ 49,580	\$ 50,994

**NOTE 6 - ACCRUED EXPENSES**

The following information is provided as of the dates indicated:

<i>(In thousands)</i>	September 30, 2018	June 30, 2018
Accrued Expenses:		
Compensation and benefits	\$ 5,668	\$ 9,394
Customer prepayments	1,865	1,070
Accrued sales commissions	1,776	2,274
Accrued warranty	7,095	6,876
Other accrued expenses	5,545	4,658
Total Accrued Expenses	\$ 21,949	\$ 24,272

**NOTE 7 - GOODWILL AND OTHER INTANGIBLE ASSETS**



The carrying values of goodwill and other intangible assets with indefinite lives are reviewed at least annually for possible impairment. The Company *may first* assess qualitative factors in order to determine if goodwill and indefinite-lived intangible assets are impaired. If through the qualitative assessment it is determined that it is more likely than *not* that goodwill and indefinite-lived assets are *not* impaired, *no* further testing is required. If it is determined more likely than *not* that goodwill and indefinite-lived assets are impaired, or if the Company elects *not to first* assess qualitative factors, the Company's impairment testing continues with the estimation of the fair value of the reporting unit using a combination of a market approach and an income (discounted cash flow) approach, at the reporting unit level. The estimation of the fair value of reporting unit requires significant management judgment with respect to revenue and expense growth rates, changes in working capital and the selection and use of an appropriate discount rate. The estimates of the fair value of reporting units are based on the best information available as of the date of the assessment. The use of different assumptions would increase or decrease estimated discounted future operating cash flows and could increase or decrease an impairment charge. Company management uses its judgment in assessing whether assets *may* have become impaired between annual impairment tests. Indicators such as adverse business conditions, economic factors and technological change or competitive activities *may* signal that an asset has become impaired.

The Company identified its reporting units in conjunction with its annual goodwill impairment testing. The Company has a total of *three* reporting units that contain goodwill. There are *two* reporting units within the Lighting Segment and *one* reporting unit within the Graphics Segment. The Company relies upon a number of factors, judgments and estimates when conducting its impairment testing including, but *not* limited to, the Company's stock price, operating results, forecasts, anticipated future cash flows and marketplace data. There are inherent uncertainties related to these factors and judgments in applying them to the analysis of goodwill impairment.

The following table presents information about the Company's goodwill on the dates or for the periods indicated:

Goodwill (In thousands)	Lighting Segment	Graphics Segment	Total
Balance as of June 30, 2018			
Goodwill	\$94,564	\$28,690	\$123,254
Accumulated impairment losses	(65,191)	(27,525)	(92,716)
Goodwill, net as of June 30, 2018	\$29,373	\$1,165	\$30,538
Balance as of September 30, 2018			
Goodwill	\$94,564	28,690	123,254
Accumulated impairment losses	(65,191)	(27,525)	(92,716)
Goodwill, net as of September 30, 2018	\$29,373	\$1,165	\$30,538

The gross carrying amount and accumulated amortization by major other intangible asset class is as follows:

Other Intangible Assets (In thousands)	September 30, 2018		
	Gross Carrying Amount	Accumulated Amortization	Net Amount
Amortized Intangible Assets			
Customer relationships	\$35,563	\$ 10,525	\$25,038
Patents	338	226	112
LED technology firmware, software	16,066	11,941	4,125
Trade name	2,658	637	2,021
Total Amortized Intangible Assets	54,625	23,329	31,296
Indefinite-lived Intangible Assets			
Trademarks and trade names	3,422	--	3,422
Total Indefinite-lived Intangible Assets	3,422	--	3,422
Total Other Intangible Assets	\$58,047	\$ 23,329	\$34,718

Other Intangible Assets (In thousands)	June 30, 2018		
	Gross Carrying Amount	Accumulated Amortization	Net Amount
Amortized Intangible Assets			
Customer relationships	\$35,563	\$ 10,011	\$25,552

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Patents	338	217	121
LED technology firmware, software	16,066	11,801	4,265
Trade name	2,658	609	2,049
Total Amortized Intangible Assets	54,625	22,638	31,987
Indefinite-lived Intangible Assets			
Trademarks and trade names	3,422	--	3,422
Total Indefinite-lived Intangible Assets	3,422	--	3,422
Total Other Intangible Assets	\$58,047	\$ 22,638	\$35,409

Page 13

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Amortization  
Expense of  
  
Other Intangible  
Assets  
  
September  
30, 2018      September  
30, 2017

Three Months Ended \$691 \$ 690

The Company expects to record annual amortization expense as follows:

*(In thousands)*

2019	\$2,069
2020	\$2,687
2021	\$2,682
2022	\$2,460
2023	\$2,412
After 2023	\$18,986

#### **NOTE 8 - REVOLVING LINE OF CREDIT**

In *February 2017*, the Company amended its secured line of credit to a \$100 million facility. The line of credit expires in the *third* quarter of fiscal 2022. Interest on the revolving line of credit is charged based upon an increment over the LIBOR rate as periodically determined, or at the bank's base lending rate, at the Company's option. The increment over the LIBOR borrowing rate, as periodically determined, fluctuates between 125 and 250 basis points depending upon the ratio of indebtedness to earnings before interest, taxes, depreciation and amortization ("EBITDA"), as defined in the line of credit agreement. The increment over LIBOR borrowing rate will remain at 175 basis points for the next *twelve* months. The fee on the unused balance of the \$100 million committed line of credit is 20 basis points. Under the terms of this line of credit, the Company has agreed to a negative pledge of real estate assets and is required to comply with financial covenants that limit the ratio of indebtedness to EBITDA and require a minimum fixed charge coverage ratio. As of *September 30, 2018*, there was \$46.2 million borrowed against the line of credit, and \$53.8 million was available as of that date. Based on the terms of the line of credit and the maturity date, the debt has been classified as long term.

The Company is in compliance with all of its loan covenants as of *September 30, 2018*.

## NOTE 9 - CASH DIVIDENDS

The Company paid cash dividends of \$1,296,000 and \$1,286,000 in the *three* months ended *September 30, 2018* and *2017*, respectively. Dividends on restricted stock units in the amount of \$31,553 and \$29,106 were accrued as of *September 30, 2018* and *2017*, respectively. These dividends will be paid upon the vesting of the restricted stock units when shares are issued to the award recipients. In *November 2018*, the Board of Directors declared a regular quarterly cash dividend of \$0.05 per share payable *November 27, 2018* to shareholders of record as of *November 16, 2018*. The indicated annual cash dividend rate is \$0.20 per share.

## NOTE 10 - EQUITY COMPENSATION

The Company's equity compensation plan, the *2012* Stock Incentive Plan ("the *2012* Plan"), was approved by shareholders in *November 2012*. The *2012* Plan covers all of the Company's full-time employees, outside directors and certain advisors and replaced all previous equity compensation plans. In *November 2016*, the Company's shareholders approved an amendment to the *2012* Plan that added *1,600,000* shares to the plan and implemented the use of a fungible share ratio that consumes 2.5 available shares for every full value share awarded by the Company as stock compensation. The *2012* Plan allows for the grant of incentive stock options, non-qualified stock options, stock appreciation rights, restricted and unrestricted stock awards, performance stock units, and other stock-based awards. Stock option grants or stock awards made pursuant to the *2012* Plan are granted at fair market value at the date of option grant or stock award.

Stock option grants may be service-based or performance-based. Service-based options granted during fiscal year 2017 and prior fiscal years generally have a four year ratable vesting period beginning one year after the date of grant. Service-based options granted during fiscal year 2018 have a three year ratable vesting period beginning one year after the date of grant. The maximum exercise period of stock options granted under the 2012 Plan is ten years. Restricted Stock Units (RSUs) granted prior to fiscal year 2018 have a four year ratable vesting period. RSUs granted during fiscal year 2018 have a three year ratable vesting period. The RSUs are non-voting, but accrue cash dividends at the same per share rate as those cash dividends declared and paid on LSI's common stock. If a stock option or RSU holder's employment with the Company terminates by reason of death, disability or retirement, as defined in the Plan, the Plan generally provides for acceleration of vesting.

In the first quarter of fiscal 2019, the Company granted Performance Stock Units (PSUs). PSUs are full value awards and consume the pool of available shares at the fungible rate of 2.5 for every full share awarded. The vesting of the PSUs is subject to the achievement of Return on Net Assets (RONA) and EBITDA objectives over a three year performance cycle. If certain one year performance objectives are met, one-third of the PSU's will vest and be released. If the one year performance objectives are not met, the entire PSU awards may be earned over the remaining three-year performance cycle.

The Company has a non-qualified deferred compensation plan providing for both Company contributions and participant deferrals of compensation. This plan is fully funded in a Rabbi Trust. All plan investments are in shares of common stock of the Company. The Company also awards its directors shares of common stock as part of their compensation. Stock compensation awards are made in the form of newly issued common shares of the Company.

In the *first* quarter of fiscal 2019, the Company granted 422,900 service-based stock options with an exercise price of \$4.94 and 134,350 PSUs at a fair value of \$4.94. In the *first* quarter of fiscal 2018, the Company granted 724,037 service-based and performance-based stock options with an exercise price of \$5.92 and 91,490 Restricted Stock Units with a fair value of \$5.92. Stock compensation expense was \$551,000 and \$984,000 in the *first* quarter of fiscal 2019 and 2018, respectively.

**NOTE 11 - SUPPLEMENTAL CASH FLOW INFORMATION**

<i>(In thousands)</i>	Three Months Ended  September 30 2018 2017
-----------------------	--

Cash payments:

Interest	\$518	\$382
Income taxes	\$(39)	\$--

Non-cash investing and financing activities:

Issuance of common shares as compensation	\$90	\$78
Issuance of common shares to fund deferred compensation plan	\$127	\$191

**NOTE 12 - COMMITMENTS AND CONTINGENCIES**

The Company is party to various negotiations, customer bankruptcies, and legal proceedings arising in the normal course of business. The Company provides reserves for these matters when a loss is probable and reasonably estimable. The Company does *not* disclose a range of potential loss because the likelihood of such a loss is remote. In the opinion of management, the ultimate disposition of these matters will *not* have a material adverse effect on the Company's financial position, results of operations, cash flows or liquidity.

The Company *may* occasionally issue a standby letter of credit in favor of *third* parties. As of *September 30, 2018*, there were *no* such standby letters of credit issued.

**NOTE 13 – SEVERANCE COSTS**

The activity in the Company's Accrued Severance Liability is as follows for the periods indicated:

<i>(In thousands)</i>	Three Months Ended September 30, 2018	Three Months Ended September 30, 2017	Fiscal Year Ended June 30, 2018
Balance at beginning of the period	\$ 1,772	\$ 235	\$235
Accrual of expense	--	--	1,900
Payments	(197 )	(159 )	(363 )
Adjustments	--	--	—
Balance at end of the period	\$ 1,575	\$ 76	\$1,772

On *April 23, 2018*, the Company's Board of Directors announced the appointment of an interim Chief Executive Officer (CEO) and Chief Operating Officer in connection with the departure of Dennis Wells, the Company's former CEO. The *\$1,772,000* severance liability reported as of *June 30, 2018* represents the severance benefits Mr. Wells is entitled to receive under his employment agreement. Of the total *\$1,575,000* reported as of *September 30, 2018*, *\$590,000* has been classified as a current liability and will be paid out over the next *twelve* months. The remaining *\$985,000* has been classified as a long-term liability.

**NOTE 14 – RESTRUCTURING COSTS**

In the *first* quarter of fiscal *2018*, management approved the closure of its *12,000* square foot leased facility in Hawthorne, California. The facility was used as a warehouse and for light assembly of light fixtures. The Company will move the light assembly to its Blue Ash, Ohio facility. The restructuring charges consist primarily of transportation costs to move inventory to Blue Ash, the impairment of equipment, costs to restore the leased facility, and severance benefits. The Company also incurred *\$435,000* related to the write-down of inventory which is *not* included in the table below. All restructuring costs are reported in cost of sales in the Lighting Segment.



The following table presents information about restructuring costs for the periods indicated:

<i>(In thousands)</i>	Three Months Ended September 30, 2018	Three Months Ended September 30, 2017
Severance benefits	\$ 19	\$ --
Moving Costs	53	--
Impairment of fixed assets and accelerated depreciation	43	--
Facility Repairs	40	--
Total	\$ 155	\$ --

The following table presents a roll forward of the beginning and ending liability balances related to the restructuring costs:

(In thousands)

	Balance as of	Restructuring Expense	Payments	Adjustments	Balance as of
	June 30,				September 30,
	2018				2018
Severance and termination benefits	\$ --	\$ 19	\$ --	\$ --	\$ 19
Other	--	93	9	--	84
Total	\$ --	\$ 112	\$ 9	\$ --	\$ 103

#### NOTE 15 – INCOME TAXES

The Company's effective income tax rate is based on expected income, statutory rates and tax planning opportunities available in the various jurisdictions in which it operates. For interim financial reporting, the Company estimates the annual income tax rate based on projected taxable income for the full year and records a quarterly income tax provision or benefit in accordance with the anticipated annual rate. The Company refines the estimates of the year's taxable income as new information becomes available, including actual year-to-date financial results. This continual estimation process often results in a change to the expected effective income tax rate for the year. When this occurs, the Company adjusts the income tax provision during the quarter in which the change in estimate occurs so that the year-to-date provision reflects the expected income tax rate. Significant judgment is required in determining the effective tax rate and in evaluating tax positions. In the *first* quarter of fiscal 2018, a deferred tax asset of \$10.7 million was created as a result of the impairment of goodwill in the Lighting reporting unit.

The Tax Cuts and Jobs Act (the "Act") was signed into law in *December 2017* and makes numerous changes to the Internal Revenue Code. Among other changes, the Act reduces the U.S. corporate income tax rate to 21% effective *January 1, 2018*. Because the Act became effective mid-way through the Company's fiscal 2018 tax year, the Company had a U.S. statutory income tax rate of 34% in the *first* quarter of fiscal 2018, before the new tax law was enacted, and will have a 21% U.S. statutory income tax rate for fiscal years 2019 and after.

Three  
Months  
Ended  
September 30  
2018 2017

**Reconciliation to effective tax rate:**

Provision for income taxes at the anticipated annual tax rate	23.0%	33.7%
Uncertain tax positions	1.3	(0.2)
Difference between deferred and current tax rate related to the impairment of goodwill	--	4.8
Shared based compensation	3.3	--
Other	--	(0.3)
<b>Effective tax rate</b>	<b>27.6%</b>	<b>38.0%</b>

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

The Company's condensed consolidated financial statements, accompanying notes and the "Safe Harbor" Statement, each as appearing earlier in this report, should be referred to in conjunction with this Management's Discussion and Analysis of Financial Condition and Results of Operations.

### **Net Sales by Business Segment**

<i>(In thousands)</i>	Three Months Ended September 30	
	2018	2017
Lighting Segment	\$61,432	\$68,428
Graphics Segment	23,525	19,038
	\$84,957	\$87,466

### **Operating Income (Loss) by Business Segment**

<i>(In thousands)</i>	Three Months Ended September 30	
	2018	2017
Lighting Segment	\$3,850	\$(22,930)
Graphics Segment	2,387	1,476
Corporate and Eliminations	(3,303)	(3,360)
	\$2,934	\$(24,814)

### **Summary Comments**

Fiscal 2019 first quarter net sales of \$84,957,000 decreased \$2.5 million or 2.9% as compared to first quarter fiscal 2018. Net sales were favorably influenced by increased net sales of the Graphics Segment (up \$4.5 million or 23.6%) more than offset by decreased net sales of the Lighting Segment (down \$7.0 million or 10.2%).

Fiscal 2019 first quarter operating income of \$2.9 million increased \$27.7 million from an operating loss of \$(24,814,000) in the first quarter of fiscal 2018. The \$27.7 million change from an operating loss in fiscal 2018 to operating income in fiscal 2019 was mostly the result of a pre-tax \$28 million goodwill impairment charge in the Lighting Segment in fiscal 2018. Adjusted fiscal 2019 operating income of \$3.5 million (which reflects the removal of plant closure costs) increased 10.6% from adjusted fiscal 2018 operating income of \$3.2 (which reflects the removal of the goodwill impairment). Refer to “Non-GAAP Financial Measures” below. The increase in adjusted operating income was the result of decreased net sales and decreased gross profit more than offset by a decrease in selling and administrative expenses. Also contributing to the period-over-period results is a one-time adjustment to the Company’s paid-time-off policy in fiscal 2019 which resulted in a favorable pre-tax adjustment to earnings of \$1.2 million.

On October 29, 2018, The Company announced that it will permanently close its New Windsor, New York manufacturing facility. The facility manufactures indoor lighting products and is included in the results of the Lighting Segment. Production will be transferred to the Company’s Erlanger, Kentucky and Blue Ash, Ohio facilities, also included in the Lighting Segment. The New Windsor facility has a workforce of 140 employees. The closure is part of ongoing actions to align the Company’s supply chain to more cost effectively serve the changing requirements of the lighting market. The closure will also allow the Company to improve utilization of existing manufacturing capacity. The transfer of production is expected to be completed by June 30, 2019.

**Non-GAAP Financial Measures**

The Company believes it is appropriate to evaluate its performance after making adjustments to the as-reported U.S. GAAP operating income, net income, and earnings per share. Adjusted operating income, net income and earnings per share, which exclude the impact of goodwill impairment and restructuring and plant closure costs, are non-GAAP financial measures. We believe that these adjusted supplemental measures are useful in assessing the operating performance of our business. These supplemental measures are used by our management, including our chief operating decision maker, to evaluate business results. We exclude these items because they are not representative of the ongoing results of operations of our business. Below is a reconciliation of these non-GAAP measures to operating income, net income, and earnings per share for the periods indicated.

(in thousands, unaudited)

	FY 2019	FY 2018
Reconciliation of operating income to adjusted operating income:		
Operating income (loss) as reported	\$2,934	\$(24,814)
Adjustment for goodwill impairment	--	28,000
Adjustment for restructuring, plant closure costs, and related inventory write-downs	590	--
Adjusted operating income	\$3,524	\$3,186

(in thousands, except per share data; unaudited)

	First Quarter		FY 2018	
	FY 2019	Diluted EPS	FY 2018	Diluted EPS
Reconciliation of net income to adjusted net income:				
Net income (loss) and earnings (loss) per share as reported	\$1,749	\$ 0.07	\$(15,629)	\$(0.61 )
Adjustment for goodwill impairment, inclusive of the income tax effect	--	--	17,363 <sup>(2)</sup>	\$0.67
Adjustment for restructuring, plant closure costs, and related inventory write-downs inclusive of the income tax effect	454 <sup>(1)</sup>	0.01	--	--
Adjusted net income and earnings per share	\$2,203	\$ 0.08	\$1,734	\$0.07

The income tax effects of the adjustments in the tables above were calculated using the estimated U.S. effective income tax rates for the periods indicated. The income tax effects were as follows (in thousands):

(1) 136

(2) 10,637

**Results of Operations**

**THREE MONTHS ENDED SEPTEMBER 30, 2018 COMPARED TO THREE MONTHS ENDED SEPTEMBER 30, 2017**

**Lighting Segment**

<i>(In thousands)</i>	Three Months Ended September 30	
	2018	2017
Net Sales	\$61,432	\$68,428
Gross Profit	\$15,475	\$18,673
Operating Income (loss)	\$3,850	\$(22,930)

Lighting Segment net sales of \$61,432,000 in the first quarter of fiscal 2019 decreased 10.2% from fiscal 2018 same period net sales of \$68,428,000. The Lighting Segment's net sales of light fixtures having solid-state LED technology totaled \$49.7 million in the first quarter of fiscal 2019 which represent 91% of total lighting product net sales. There continues to be a reduction in the Company's traditional lighting sales (metal halide and fluorescent light sources) as customers convert from traditional lighting to light fixtures having solid-state LED technology.

Gross profit of \$15,475,000 in the first quarter of fiscal 2019 decreased \$3.2 million or 17.1% from the same period of fiscal 2018, and decreased from 27.0% to 25.0% as a percentage of Lighting Segment net sales (customer plus inter-segment net sales). The Company incurred restructuring and plant closure costs that were recorded in cost of sales related to the closure of its Hawthorne, California facility of \$590,000 in fiscal 2019 with no comparable costs in fiscal 2018. The remaining decrease in amount of gross profit is due to the effect of reduced sales volume, competitive pricing pressures, and inflationary pressures of certain commodities, partially offset by manufacturing efficiencies as a result of the Company's lean initiatives.

Selling and administrative expenses of \$11,625,000 in the first quarter of fiscal year 2019 decreased \$30 million from the same period of fiscal 2018 selling and administrative expenses of \$41,603,000, primarily due to the \$28 million goodwill impairment charge in fiscal 2018. When the goodwill impairment charge is removed from fiscal 2018 results, there was a \$2.0 million or 14.4% reduction in selling and administrative expenses. The reduction in selling and administrative expenses is mostly driven by lower commission expense which is due to lower sales volume and a reduction of wage and benefit expense.

The Lighting Segment first quarter fiscal 2019 operating income of \$3,850,000 increased \$26.8 million from an operating loss of \$(22,930,000) in the same period of fiscal 2018 primarily due to a \$28 million pre-tax goodwill impairment charge. When the impact of the goodwill charge is removed from fiscal 2018 results and the restructuring and plant closure costs of \$590,000 are removed from the fiscal 2019 results, fiscal 2019 adjusted operating income of \$4,440,000 was \$630,000 lower than fiscal 2018 adjusted operating income of \$5,070,000. The reduction in sales volume and gross profit was partially offset by lower selling and administrative expenses.

## Graphics Segment

<i>(In thousands)</i>	Three Months	
	Ended	
	September 30	
	2018	2017
Net Sales	\$23,525	\$19,038
Gross Profit	\$5,782	\$5,063
Operating Income	\$2,387	\$1,476

Graphics Segment net sales of \$23,525,000 in the first quarter of fiscal 2019 increased \$4.5 million or 23.6% from fiscal 2018 same period net sales of \$19,038,000. Most of the increase in sales is from growth in sales to the Petroleum and Quick Service Restaurant markets including digital technology.

Gross profit of \$5,782,000 in the first quarter of fiscal 2019 increased \$0.7 million or 14.2% from the same period of fiscal 2018. Gross profit as a percentage of segment net sales (customer plus inter-segment net sales) decreased from



26.6% in the first quarter of fiscal 2018 to 24.5% in the first quarter of fiscal 2019. The change in amount of gross profit is due to the net effect of increased net sales (customer plus inter-segment net sales) partially offset by a change in product mix. Also contributing to the year-over-year change in gross profit was a \$0.6 million increase in overhead spending mostly driven by an increase in wage expense.

Selling and administrative expenses of \$3,395,000 in the first quarter of fiscal 2019 decreased \$0.2 million or 5.4% from the same period of fiscal 2018 primarily as a result of decreased wage and benefit expense.

The Graphics Segment first quarter fiscal 2019 operating income of \$2,387,000 increased \$0.9 million or 61.7% from operating income of \$1,476,000 in the same period of fiscal 2018. The net increase of \$0.9 million was primarily the net result of increased net sales, increased gross profit, decreased gross profit margin as a percentage of sales, and decreased selling and administrative expenses.

### Corporate and Eliminations

<i>(In thousands)</i>	Three Months Ended September 30	
	2018	2017
Gross Profit (Loss)	\$4	\$(33 )
Operating (Loss)	\$(3,303)	\$(3,360)

The gross profit or loss relates to the elimination of intercompany profit in inventory.

Administrative expenses of \$3,307,000 in the first quarter of fiscal 2019 decreased slightly from the same period of the prior year. The change is primarily the result of a decrease in employee compensation and benefit expense (\$0.6 million) offset by an equal an increase in outside service expense (\$0.4 million), and a net increase in various other expense categories (\$0.2 million).

## **Consolidated Results**

The Company reported \$518,000 net interest expense in the first quarter of fiscal 2019 compared to \$403,000 net interest expense in the first quarter of fiscal 2018. The change from interest expense from fiscal 2018 to fiscal 2019 is the result of higher interest rates on the Company's line of credit and higher commitment fees on its unused portion of the line of credit.

The \$667,000 income tax expense in the first quarter of fiscal 2019 represents a consolidated effective tax rate of 27.6% influenced by certain permanent book-tax differences and by an expense related to uncertain income tax positions. The \$9,588,000 income tax benefit in the first quarter of fiscal 2018 represents a consolidated effective tax rate of 38% influenced by the goodwill impairment.

The Company reported a net income of \$1,749,000 in the first quarter of fiscal 2019 compared to a net loss of \$(15,629,000) in the same period of the prior year. The change between a net loss in fiscal 2018 to net income in fiscal 2019 is mostly driven by the \$28 million pre-tax goodwill impairment charge in fiscal 2018 with no comparable event in fiscal 2019. When the impact of the fiscal 2018 goodwill impairment charge and the fiscal 2019 restructuring and plant costs are removed from the reported results, the fiscal 2019 adjusted net income of \$2,203,000 increased \$0.5 million or 27% from fiscal 2018 adjusted net income of \$1,734,000. The change in adjusted net income is primarily the net result of decreased net sales, decreased gross profit, decreased selling and administrative expenses, increased interest expense, and a lower tax rate. Diluted earnings per share of \$0.07 was reported in the first quarter of fiscal 2019 as compared to \$(0.61) diluted loss per share in the same period of fiscal 2018. The weighted average common shares outstanding for purposes of computing diluted earnings per share in the first quarter of fiscal 2019 were 26,365,000 shares as compared to 25,791,000 shares in the same period last year.

## **Liquidity and Capital Resources**

The Company considers its level of cash on hand, borrowing capacity, current ratio and working capital levels to be its most important measures of short-term liquidity. For long-term liquidity indicators, the Company believes its ratio of long-term debt to equity and its historical levels of net cash flows from operating activities to be the most important

measures.

At September 30, 2018, the Company had working capital of \$72.6 million, compared to \$67.9 million at June 30, 2018. The ratio of current assets to current liabilities was 2.59 to 1 as compared to a ratio of 2.61 to 1 at June 30, 2018. The \$4.7 million increase in working capital from June 30, 2018 to September 30, 2018 was primarily related to the net effect of increased cash and cash equivalents (\$1.0 million), increased net accounts receivable (\$9.2 million), decreased net inventory (\$1.4 million), an increase in accrued expenses (\$2.3 million), a decrease in refundable income taxes (\$0.6 million), and an increase in accounts payable (\$5.8 million). The \$4.1 million of the increase in accounts receivable is the result of the adoption of the new revenue guidance. The Company has a strategy of aggressively managing working capital, including reduction of the accounts receivable days sales outstanding (DSO) and reduction of inventory levels, without reducing service to its customers.

The Company generated \$2.2 million of cash from operating activities in the first quarter of fiscal 2019 as compared to a use of cash of \$2.7 million in the same period of the prior year. This \$4.9 million increase in net cash flows from operating activities is primarily the net result of an increase rather than a decrease in accounts payable (favorable change of \$7.3 million), a smaller increase in net accounts receivable (favorable change of \$1.2 million), an increase rather than a decrease in net inventory (unfavorable change of \$4.2 million), a smaller decrease in refundable income taxes (favorable change of \$0.2 million), an increase in customer prepayments (favorable change of \$0.4 million), and an increase in net income in fiscal 2019 from a net loss in fiscal 2018 offset by several non-cash add-backs (favorable change of \$0.4 million).

Net accounts receivable were \$59.8 million and \$50.6 million at September 30, 2018 and June 30, 2018, respectively. DSO increased to 59 days at September 30, 2018 from 53 days at June 30, 2018. The Company believes that its receivables are ultimately collectible or recoverable, net of certain reserves, and that aggregate allowances for doubtful accounts are adequate.

Net inventories of \$49.6 million at September 30, 2018 decreased \$1.4 million from \$51.0 million at June 30, 2018. The decrease of \$1.4 million is the result of a decrease in gross inventory of \$0.9 million and an increase in obsolescence reserves of \$0.5 million. Based on a strategy of balancing inventory reductions with customer service and the timing of shipments, net inventory increased 1.8 million in the first quarter of fiscal 2019 in the Graphics Segment which was more than offset by a decrease in net inventory in the Lighting Segment of \$3.2 million.

Cash generated from operations and borrowing capacity under the Company's line of credit is the Company's primary source of liquidity. The Company has a secured \$100 million revolving line of credit with its bank, with \$46.1 million of the credit line available as of October 29, 2018. This line of credit is a \$100 million five year credit line expiring in the third quarter of fiscal 2022. The Company believes that its \$100 million line of credit plus cash flows from operating activities are adequate for the Company's fiscal 2019 operational and capital expenditure needs. The Company is in compliance with all of its loan covenants.

The Company used cash of \$0.7 million related to investing activities in the first quarter of fiscal 2019 as compared to a source of \$1.0 million in the same period of the prior year, resulting in an unfavorable change of \$1.7 million. Capital expenditures for the first quarter of fiscal 2019 increased \$0.2 million to \$0.6 million from the same period in fiscal 2018. The Company sold its Woonsocket manufacturing facility for \$1.5 million in the first quarter of fiscal 2018 which contributed to the change in cash flow from investing activities from fiscal 2018 to fiscal 2019.

The Company used \$0.6 million of cash related to financing activities in the first quarter of fiscal 2019 compared to a source of cash of \$0.8 million in the first quarter of fiscal 2018. The \$1.3 million unfavorable change in cash flow was the net result of borrowings in excess of payments of long term debt of \$1.4 million.

The Company has, or could have, on its balance sheet financial instruments consisting primarily of cash and cash equivalents, short-term investments, revolving lines of credit, and long-term debt. The fair value of these financial instruments approximates carrying value because of their short-term maturity and/or variable, market-driven interest rates.

### **Off-Balance Sheet Arrangements**

The Company has no financial instruments with off-balance sheet risk and has no off-balance sheet arrangements, except for various operating leases. However, none of these operating leases, individually or in the aggregate have or are reasonably likely to have a current effect on the Company's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources that is material.

## **Cash Dividends**

In November 2018, the Board of Directors declared a regular quarterly cash dividend of \$0.05 per share payable November 27, 2018 to shareholders of record as of November 16, 2018. The indicated annual cash dividend rate for fiscal 2019 is \$0.20 per share. The Board of Directors has adopted a policy regarding dividends which indicates that dividends will be determined by the Board of Directors in its discretion based upon its evaluation of earnings, cash flow requirements, financial condition, debt levels, stock repurchases, future business developments and opportunities, and other factors deemed relevant.

## **Critical Accounting Policies and Estimates**

A summary of the Company's significant accounting policies is included in Note 1 to the audited consolidated financial statements of the Company's fiscal 2018 Annual Report on Form 10-K.

## **New Accounting Pronouncements**

In February 2016, the Financial Accounting Standards Board issued ASU 2016-02, "Leases." The amended guidance requires an entity to recognize assets and liabilities that arise from leases. The amended guidance is effective for financial statements issued for fiscal and interim periods within those years, beginning after December 15, 2018, or the Company's fiscal 2020, with early adoption permitted. The Company has not yet determined the impact the amended guidance will have on its financial statements.

## **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

There have been no material changes in the Company's exposure to market risk since June 30, 2017. Additional information can be found in Item 7A, Quantitative and Qualitative Disclosures About Market Risk, which appears on page 13 of the Annual Report on Form 10-K for the fiscal year ended June 30, 2018.

## **ITEM 4. CONTROLS AND PROCEDURES**

### **Disclosure Controls and Procedures**

The Company maintains disclosure controls and procedures (as such term is defined Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”)), that are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized and reported within required time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

We conducted, under the supervision of our management, including the Chief Executive Officer and Chief Financial Officer, an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934. Based upon our evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of September 30, 2018, our disclosure controls and procedures were effective. Management believes that the condensed consolidated financial statements included in this Quarterly Report on Form 10-Q are fairly presented in all material respects in accordance with GAAP for interim financial statements, and the Company’s Chief Executive Officer and Chief Financial Officer have certified that, based on their knowledge, the condensed consolidated financial statements included in this report fairly present in all material respects the Company’s financial condition, results of operations and cash flows for each of the periods presented in this report.

### **Changes in Internal Control**

During the quarter ended September 30, 2018, the Company enacted additional controls related to the adoption of ASU 2014-09, “Revenue from Contracts with Customers (Topic 606).” There have been no changes in the Company’s internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter ended September 30, 2018, that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting, except as otherwise described in this Item 4.

**PART II. OTHER INFORMATION**

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

NONE

**ITEM 6. EXHIBITS**

Exhibits:

10.1 Nonqualified Stock Option Agreement for Inducement Awards between the Company and James A. Clark dated November 1, 2018

10.2 Restrictive Covenant and Confidentiality Agreement executed by James A. Clark dated November 1, 2018

31.1 Certification of Principal Executive Officer and Principal Financial Officer required by Rule 13a-14(a)

32.1 Section 1350 Certification of Principal Executive Officer and Principal Financial Officer

101.INS XBRL Instance Document

101.SCH XBRL Taxonomy Extension Schema Document

101.CAL XBRL Taxonomy Extension Calculation Linkbase Document

101.DEF XBRL Taxonomy Extension Definition Linkbase Document

101.LAB XBRL Taxonomy Extension Label Linkbase Document

101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

**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.

**LSI Industries Inc.**

By: /s/ James E. Galeese  
James E. Galeese  
Executive Vice President and Chief

Financial Officer  
(Principal Executive Officer and

Principal Financial Officer)