The Image Company

LIGHTING

GRAPHICS

SOLUTIONS *plus*

TECHNOLOGY

2004
Annual
Report

LSI Industries is an integrated design, manufacturing and technology company supplying its own high quality lighting fixtures, graphics elements and narrowcast digital messaging for both exterior and interior applications. The Company's Lighting Segment produces high performance products dedicated to outdoor, architectural outdoor, indoor, architectural indoor and accent/downlight applications. The Graphics Segment provides a vast array of products and services, including signage, menu board systems, narrowcasting, decorative fixturing, design support, and engineering and project management for custom programs for today's retail environment. LSI's major markets are the petroleum/convenience store, multi-site retail (including automobile dealerships, restaurants and national retail accounts) and the commercial/industrial lighting markets.

LSI Creates a New Image

What: LSI Industries is launching a new web site

Where: *www.lsi-industries.com*

When: End of September, 2004...be sure to check our current web site for the exact date

Why: Because Image is Everything!

Contents

Financial Highlights	1
Opportunity Everywhere	foldout
Chairman's Letter	2
Management's Discussion and Analysis of Financial Condition and Results of Operations	6
Financial Statements	14
Notes to Consolidated Financial Statements	19
Report of Independent Registered Public Accounting Firm	30
Report of Management	30
Selected Financial Data	31
Corporate Information and Operating Facilities	32
Board of Directors, Corporate Officers and Executive Management	Inside Back Cover

"Safe Harbor" Statement under the Private Securities Litigation Reform Act of 1995

This Annual Report 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," "should" and similar expressions, and the negative version thereof, and by the context in which they are used. Such statements are based upon current expectations of the Company and speak only as of the date made. Risks and uncertainties include, but are not limited to, the impact of competitive products and services, product demand and market acceptance risks, reliance on key customers, financial difficulties experienced by customers, the adequacy of reserves and allowances for doubtful accounts, fluctuations in operating results or costs, unexpected difficulties in integrating acquired businesses, and the ability to retain key employees of acquired businesses. The Company has no obligation to update any forward-looking statements to reflect subsequent events or circumstances.

OPPORTUNITY

Lighting, Graphics, Technology = Image

Accent Lighting

Interior Lighting

Interior Graphics

Narrowcasting

Parking Garage Lighting

Pedestrian Scale Lighting

Flood Lighting

Landscape Lighting

EVERYWHERE

The Markets We Serve with the Products We Make-

Indoor and Outdoor Lighting and Graphics; Narrowcasting

Casual Dining
Quick Service Restaurant
Financial Services
Automobile

Petroleum C-Store
Supermarkets
Hotel/Motel
Drug Store

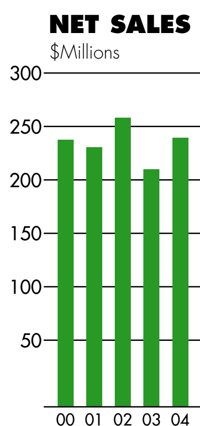
Retail
- Specialty
- Big Box
- Department Store

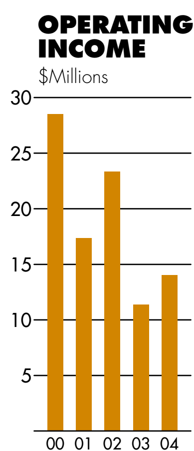
Brand Programs

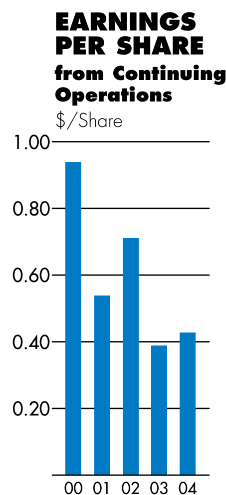
Sports
Manufacturing
Commercial Properties
Schools

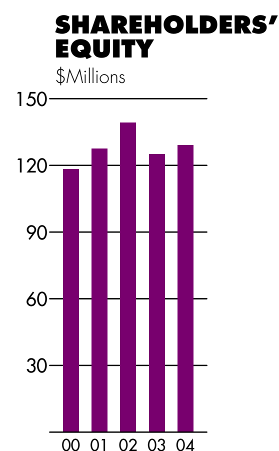
FINANCIAL HIGHLIGHTS

	2004	2003	2002
INCOME STATEMENT DATA *(In thousands, except per share)*			
Net sales	$241,405	$213,133	$259,261
Operating income	$ 14,034	$ 11,366	$ 23,384
Income from continuing operations before cumulative effect of accounting change	$ 8,690	$ 7,793	$ 14,186
Net income (loss)	$ 8,690	$ (10,748)	$ 14,186
Earnings (losss) per common share			
Basic			
Earnings per share from continuing operations before cumulative effect of accounting change	$ .44	$ .39	$ .72
Earnings (loss) per share	$ .44	$ (.55)	$ .72
Diluted			
Earnings per share from continuing operations before cumulative effect of accounting change	$ .43	$ .39	$ .71
Earnings (loss) per share	$ .43	$ (.54)	$ .71
BALANCE SHEET DATA *(In thousands)*			
Working capital	$ 64,724	$ 59,633	$ 55,793
Total assets	$174,732	$162,776	$189,842
Long-term debt, including current maturities	$ 11,554	$ 14,084	$ 18,053
Shareholders' equity	$128,863	$124,905	$139,349
CASH FLOW DATA *(In thousands)*			
Capital expenditures	$ 4,708	$ 5,452	$ 16,846
Depreciation and amortization	$ 5,925	$ 5,702	$ 6,096









DEAR SHAREHOLDERS

We finished fiscal 2004 with net sales 13% higher than the prior fiscal year; operating income and income before taxes increased 23%. Fiscal 2004 income before cumulative effect of accounting change was $8.7 million ($0.43 per share), an increase of 12% from the $7.8 million ($0.39 per share) reported for fiscal 2003. Of course, operating results and business developments including our successes, disappointments, and challenges have been reported to shareholders in some detail throughout the fiscal year. Make no mistake, even though sales and earning increased over the prior fiscal year we did not achieve our internal profit goals (sales objectives were exceeded) for fiscal 2004.

Rather than review the many general business activities and accomplishments of fiscal 2004 and the particular factors that depressed earnings, all of which have previously been reported and discussed, I will use this President's letter to tell you why I believe the future is so positive for LSI Industries. It is sometimes easy to forget that we measure companies on a quarterly and yearly basis as a matter of convenience, yet true business strategies are implemented over the course of not one or two but several years. And so it is with LSI Industries.

My conviction as it relates to our favorable outlook and future is based on a broad range of strengths including dedicated and highly capable employees, strong customer relationships, innovative new products, a seasoned and success oriented management team, external growth through acquisitions, a conservative and sound balance sheet, and more. All of these elements are realities at LSI Industries, yet they do not by themselves represent the principal reason for the strength and optimism that I feel.

As I see it, LSI Industries is now beginning to enjoy the converging results of a number of strategies, plans and directions that were started several years ago to lessen our dependence on the petroleum market. These changes are now fundamental to how the company approaches its marketplace. What are these strategic directions? Basically, there are five main strategies that guide the Company's direction. Some go back to LSI's founding over 28 years ago and are best thought of as bedrock operating and growth strategies. Others have been identified and implemented in more recent years. All have proven to be effective and important in our continued growth and profitability.

COMBINING 100 YEARS OF LIGHTING EXPERIENCE WITH UNBEATABLE SERVICE

LIGHTING

LSI Lighting Solutions *Plus* combines decades of lighting experience with the highest level service to help our customers make their lighting projects as effective as they can be. Our lighting group offers extensive product lines, including Outdoor, Architectural Outdoor, Indoor, Architectural Indoor and Accent & Downlight lighting.

LSI Lighting Solutions *Plus* provides service capabilities and strategically located manufacturing and distribution facilities, all focused on meeting the product and service needs that are critical to our customers.

GRAPHICS

LSI Graphic Solutions *Plus* produces and manages image and brand programs for a diverse group of customers. Markets include petroleum/convenience store, retail, financial, restaurant, grocery, drug and automotive. LSI Graphic Solutions *Plus* also offers products like menu board and information delivery systems, and active digital signage with the LSI Narrowcasting solution.

The graphics operation presents every customer with the finest in manufacturing techniques and capabilities as well as project management, value engineering, design support, inventory management and installation services. LSI Graphic Solutions *Plus* can deliver on every aspect of a store image program, from wall murals and department signage, to architectural elements and fixture displays.

UNIFIED GRAPHIC CAPABILITIES THAT ARE SECOND TO NONE

More specifically, generally in chronological order, they are as follows:

- **To capture a commanding share of specialized niche markets.** LSI got its start by providing outdoor lighting systems to the petroleum/convenience store market and later additional niche markets, including quick service restaurants and automotive dealerships. This early strategy remains viable and allows a high level of customer service combined with specialized products to produce above average growth and profit margins. Our leading presence in selected niche markets will continue to contribute to overall growth and profits, especially when the major oil companies return to their re-imaging programs.
- **To operate as a low cost producer.** This is an on-going behind the scenes strategy from an operations viewpoint. We continually examine better and more efficient ways to produce high-quality products at the lowest reasonable costs. Our investments in new manufacturing technologies and capital equipment will keep us on the forefront of low cost production and high quality output.
- **To capitalize on the core strategy of "Lighting + Graphics + Technology = Complete Image Solutions."** This value proposition theme for our customers runs deep throughout LSI and has been highly successful. It allows LSI to approach its markets with "one-stop" capabilities that leverages our relative importance with customers and provides a significant competitive advantage. This key strategy started out with "Lighting + Graphics = Image" and, through the years, has been expanded and refined to its current state, which now can be expressed as a fully integrated offering of lighting, graphics, and technology products and services beginning with design, and progressing through engineering, manufacturing, installation, and support. This is being implemented through the concepts of LSI Lighting Solutions Plus and LSI Graphics Solutions Plus, whereby we are strengthening the "LSI" brand in the markets we serve.
- **To expand our presence in the large commercial and industrial lighting markets.** This strategy allows LSI to diversify our legacy dependence on the petroleum and specialty niche markets by increasing our presence in much larger markets having different business cycles. The effort is to reduce our overall business risk and enhance growth opportunities, albeit usually at somewhat reduced profit margins. Had we not implemented this strategy, which was made possible by broadening our product line offerings through several acquisitions, operating results

during the past three years would have suffered. We now have an opportunity to grow the commercial and industrial lighting platform as well as a highly effective capability in specialty niche markets.

- **To always remain financially sound.** This would not usually be thought of as a strategy, but it clearly is to my way of thinking. A conservative and sound balance sheet coupled with strong cash flow from operations allows management great flexibility in dealing with changing market conditions and developing and pursuing new operating and growth strategies. LSI will continue this policy. At June 30, 2004 our current ratio was 3 to 1, long-term debt was $11.6 million and shareholders' equity was $128.9 million. We intend to continue our growth, both internally and through acquisitions, and have the balance sheet, cash flow, and bank credit facility to do so.

My view is that LSI Industries is in a strong position to capitalize on its opportunities and, furthermore, its opportunities have never been as great as they are today. I am, of course, aware that shareholders measure success largely on the basis of share price and total return which includes cash dividends. As a major shareholder of LSI, share price and dividends are also important to me. During fiscal 2004 we paid cash dividends of $0.264 per share, an increase of 38% over the prior year, and as fiscal 2004 ended, our share price was up 30%, or $2.62 per share. Since then, our share price has declined about 13% largely, I believe, based on our fourth quarter operating results. As fiscal 2005 unfolds, I am optimistic that our higher cash dividend payout ratio, coupled with higher earnings and a planned proactive program to educate the financial community about LSI's new direction, will result in positive returns to our shareholders.

I look forward to fiscal 2005 and beyond with confidence knowing our strategies are working and we have a solid plan for growth. We are proud of our internal and marketing accomplishments during fiscal 2004 and prior years, confident in the knowledge that we have built a solid base for expansion.

To our shareholders, employees, sales representatives, customers, and suppliers, thank you for your work and support.

Sincerely,

Robert J. Ready
Chairman, President and CEO

NARROWCASTING COMBINED WITH LIGHTING AND GRAPHICS DELIVERS TECHNOLOGY DRIVEN SOLUTIONS

TECHNOLOGY

The LSI Narrowcasting solution is an intelligent system that manages the distribution of digital media content, in turn delivering high impact messaging that prompts targeted audience segments to take action.

LSI Industries is working with customers to identify and leverage the key drivers of their retail merchandising and promotional success, and incorporate these elements into a customized Narrowcasting program that increases their sales.

FINANCIAL RESULTS

Management's Discussion and Analysis of Financial Condition and Results of Operations......6

Financial Statements 14

Notes to Consolidated Financial Statements...........19

Report of Independent Registered Public Accounting Firm 30

Report of Management..30

Selected Financial Data 31

NET SALES BY BUSINESS SEGMENT

(In thousands)	**2004**	2003	2002
Lighting Segment	**$159,748**	$136,076	$147,930
Graphics Segment	**81,657**	77,057	111,331
	$241,405	$213,133	$259,261

RESULTS OF OPERATIONS

The Company reorganized into two new reportable business segments at the beginning of fiscal 2004. As a result, fiscal years 2002 and 2003 have been revised to reflect these two new segments: the Lighting Segment and the Graphics Segment. All share and per share data reflect the 5-for-4 stock split which was effective November 14, 2003.

2004 Compared To 2003

Net sales of $241,405,000 in fiscal 2004 increased 13% from fiscal 2003 net sales of $213,133,000. Lighting Segment net sales increased $23.7 million, or 17%, to $159.7 million and Graphics Segment net sales increased $4.6 million, or 6%, to $81.7 million as compared to the prior year. Sales to the petroleum/convenience store market, the Company's largest market representing 28% and 29% of fiscal 2004 and 2003 net sales, respectively, were up 9% over fiscal 2003 to $66.5 million. Net sales to this market are reported in both the Lighting and Graphics Segments, depending upon the product or service sold. While sales to this market have increased this year, the Company believes concerns about the Middle East and the war with Iraq have had the effect of reducing major image program spending by the major oil companies. The petroleum/convenience store market has been, and will continue to be, a very important niche market for the Company.

The $23.7 million increase in Lighting Segment net sales is primarily the result of an approximate $10.2 million increase in sales to the commercial/industrial lighting markets (resulting, in part, from a slight improvement in the economy, as well as good response from the Company's new independent commercial sales representatives), and an aggregate increase of $12.4 million of lighting sales to our niche markets of petroleum/convenience store, automotive dealerships, quick service restaurants, and retail national accounts (including increased sales to a major national retailer).

The $4.6 million increase in Graphics Segment net sales is primarily the result of the net effect of increased graphics sales to the petroleum/convenience store market ($3.2 million), increased sales to a retail store customer (approximately $9.5 million), and reduced menu board system sales (one quick service restaurant customer sales are down $6.4 million as their roll out program is now considered complete).

Image and brand programs, whether full conversions or enhancements, are important to the Company's strategic direction. Image programs include situations where our customers refurbish their retail sites around the country by replacing some or all of the lighting, graphic elements, menu board systems and possibly other items they may source from other suppliers. These image programs often take several quarters to complete and involve both our customers' corporate-owned sites as well as their franchisee-owned sites, the latter of which involve separate sales efforts by the Company with each franchisee. Brand programs typically occur as new products are offered or new departments are created within an existing retail store. Relative to net sales to a customer before and after an image or brand program, net sales during the program are typically significantly higher, depending upon how much of the lighting, graphics or menu board business is awarded to the Company. Sales related to a customer's image or brand program are reported in either the Lighting Segment and/or the Graphics Segment, depending upon the product and/or service provided.

While sales prices in some markets that the Company serves were increased in the second half of the year, inflation did not have a significant impact on sales in fiscal 2004. The Company experienced competitive pricing pressures in most markets, thereby holding price increases to a minimum. In some markets the Company was able to increase sales prices to recover increased raw material costs, but generally with little or no increase in gross profit. The

rise in steel and aluminum prices caused a reduction in the gross profit margin. Additionally, during this period of transition to an improving economy, in certain situations the Company has accepted lower-than-normal sales prices and lower-than-normal margins where necessary, in part to protect and grow market share.

Gross profit of $59,522,000 in fiscal 2004 increased 8% from last year, but decreased as a percentage of net sales to 24.7% in fiscal 2004 as compared to 25.9% last year. The increase in amount of gross profit is due primarily to the 13% increase in net sales, product mix and efficiencies, partially offset by higher installation, freight and distribution expenses. While the Company instituted sales price increases in the second half of fiscal 2004, manufacturing wages and compensation increases that were two percentage points greater than the increase in net sales, competitive pricing pressures throughout the year and increasing material costs in the second half contributed to the decreased gross profit margin percentage. Selling and administrative expenses increased $1.7 million. Fiscal 2004 had $0.8 million lower bad debt expense (in fiscal 2003 the Graphics Segment had significant additional expense due primarily to customer bankruptcies and cash flow difficulties), lower legal and professional fees ($0.2 million), and lower travel expense ($0.2 million). Items offsetting this reduction of expense were increased employee compensation ($1.7 million due to increased salary rates, and increased staffing levels and incentive compensation) and outside consultant expenses ($0.7 million) related to the Company's implementation of JD Edwards OneWorld business operating system in the Cincinnati and Kentucky operations and to the documentation and testing of internal controls.

The Company reported interest expense of $260,000 in fiscal 2004 as compared to $378,000 last year. The change between years is reflective of both reduced interest rates and reduced average outstanding borrowings on the Company's line of credit. The effective tax rate in fiscal 2004 was 37.0%. The fiscal 2003 effective tax rate of 30.7% is the net result of a normal tax provision of about 37.5% that was reduced when the Company recorded federal and state income tax credits.

Income before cumulative effect of an accounting change was $8,690,000 in fiscal 2004, a 12% increase as compared to $7,793,000 in fiscal 2003. The increase is primarily the result of increased gross profit on increased net sales and decreased interest expense, partially offset by increased operating expenses and income taxes. Diluted earnings per share, before the cumulative effect of an accounting change, was $0.43 in fiscal 2004 as compared to $0.39 per share in fiscal 2003. The weighted average common shares outstanding for purposes of computing diluted earnings per share in fiscal 2004 was 20,038,000 shares as compared to 19,923,000 shares last year.

The Company completed the transitional goodwill impairment test required by Statement of Financial Accounting Standards No. 142 (SFAS No. 142), "Goodwill and Other Intangible Assets," as of July 1, 2002. This test required the Company, through an independent appraisal firm, to assess the fair value, as determined on a discounted cash flow basis, of each reporting unit that had goodwill on its balance sheet, and compare that value to the carrying value of the reporting unit's net assets as of July 1, 2002. The Company determined for the fiscal 2003 transitional goodwill impairment test that it had eight reporting units, each of which represented an acquired business that operated in the organizational structure one level below the business segment level. Based upon this analysis, there was full impairment of the recorded net goodwill of two reporting units in the Lighting Segment (totaling $23,593,000) and one reporting unit in the Graphics Segment (totaling $929,000). The impairment of $24,522,000, a non-cash and non-operating charge, was booked in the amount of $18,541,000, net of income taxes, as a change in accounting method and was recorded as of the date of adoption of SFAS No. 142, July 1, 2002. The Company has determined that it will perform its annual goodwill impairment test in accordance with SFAS No. 142 as of July 1st each year. There were no changes in accounting methods and no impairment of goodwill in fiscal 2004.

The Company recorded net income of $8,690,000 in fiscal 2004 as compared to a net loss of $10,748,000 in fiscal 2003. The increase in 2004 is the result of the $18,541,000 goodwill impairment loss that was recorded as an accounting change in fiscal 2003, plus the increased fiscal 2004 income before cumulative effect of accounting change. Diluted earnings or (loss) per share was $(0.54) in fiscal 2003 as compared to $0.43 per share in fiscal 2004.

2003 Compared To 2002

Net sales of $213,133,000 in fiscal 2003 decreased 18% from fiscal 2002 net sales of $259,261,000. Lighting Segment net sales decreased 8% to $136.1 million and Graphics Segment net sales decreased 31% to $77.0 as compared to the prior year. Net sales to the petroleum/convenience store market represented 29% and 34% of total net sales in 2003 and fiscal 2002, respectively. Sales to this market decreased $25.8 million in the fiscal 2003 as compared to fiscal 2002 due both to general economic conditions in this market and to much lower volume (down $9.6 million) associated with an image conversion program of a major oil company. The Company believes concerns about the Middle East and the war with Iraq have had the effect of reducing spending by the major oil companies. The Company believes this reduction constitutes a short term, rather than a long term trend. The petroleum/convenience store market has been, and will continue to be, a very important niche market for the Company.

The decrease in Lighting Segment net sales is primarily attributed to lower lighting sales to the petroleum/convenience store market. Also contributing to the decrease in Lighting Segment net sales is economic weakness in the commercial/industrial market, and, to an unknown degree, to several manufacturer sales representative agency changes made by the Company during fiscal 2003. The Company believes these changes, which are now complete, will have a long term effect of increasing net sales through utilization of a more experienced and effective representative sales force, but a short term effect in fiscal 2003 of a possible reduction in net sales as the new sales representative agencies are fully indoctrinated to the Company and trained in its lighting products.

The decrease in Graphics Segment net sales is primarily attributed to continued weakness in the petroleum/convenience store market. Additionally, net sales of the significant menu board program originally scheduled to conclude in the second quarter were down $14.8 million as compared to last year. The Company expects some additional sales through the first half of fiscal 2004 as the remaining franchisee-operated restaurants of this customer implement this new menu board system. Image conversion programs include situations where our customer refurbishes its retail sites around the country by replacing some or all of the lighting, graphic elements, menu board systems and possibly other items they may source from other suppliers. These image conversions take several quarters to complete and involve both our customer's corporate-owned sites as well as its franchisee-owned sites, the latter of which involve separate sales efforts by the Company with each franchisee. Relative to net sales to this customer before and after the image conversion program, net sales during the image conversion are typically significantly higher, depending upon how much of the lighting, graphics or menu board business is awarded to the Company.

While sales prices in some markets that the Company serves were increased, inflation did not have a significant impact on sales in fiscal 2003 as competitive pricing pressures held price increases to a minimum. During this temporary period of economic weakness, in certain situations the Company has accepted lower-than-normal sales prices and lower-than-normal margins where necessary, in part to protect market share.

Gross profit of $55,167,000 in fiscal 2003 decreased 24% from last year, and decreased as a percentage of net sales to 25.9% in fiscal 2003 as compared to 27.9% last year. The decrease in amount of gross profit is due primarily to the 18% decrease in net sales, product mix and competitive pressures. These factors offset the approximate net $5.5 million of cost reductions and improvements the Company has achieved in manufacturing overhead spending, about 78% of which was in the area of wages, incentive compensation and benefits which are also related to the decrease in net sales and lower employment levels. Selling and administrative expenses decreased $5.2 million

or 11%. About 70% of this reduction relates to lower compensation and benefits costs as a result of the Company's reduced sales volume and profitability. About $1.2 million of the reduction is due to lower sales commissions that relate almost entirely to the Company's lighting sales. The Company adopted Financial Accounting Standards Statement No. 142 effective July 1, 2002, and accordingly did not record any goodwill amortization expense in fiscal 2003. Fiscal 2002 selling and administrative expense includes $1,349,000 of goodwill amortization expense. As a percentage of net sales, selling and administrative expenses were at 20.6% in fiscal 2003 as compared to 18.9% last year.

The Company reported interest expense of $378,000 in fiscal 2003 as compared to $575,000 last year. The change between years is primarily reflective of both reduced interest rates and average outstanding borrowings on the Company's line of credit that were about 24% less in fiscal 2003 as compared to last year, partially offset by about $92,000 of interest that was capitalized in fiscal 2002 related to the Company's construction of a manufacturing facility in New York. The increase in interest income in fiscal 2003 is reflective of interest income recorded on a note receivable from one of the Company's customers in the Graphics Segment. The effective tax rate in fiscal 2003 was reduced to 30.7%, compared to 37.9% last year, primarily as a result of the Company recording federal and state income tax credits that had not previously been recognized, as well as a lower federal income tax rate reflective of the lower taxable income, and a lower effective state income tax rate as a result of credits and improved filing methods.

Income before cumulative effect of an accounting change was $7,793,000 in fiscal 2003, a 45% decrease as compared to $14,186,000 in fiscal 2002. The decrease is primarily the result of decreased gross profit from decreased net sales, partially offset by decreased operating expenses, net interest expense and income taxes. Diluted earnings per share, before the cumulative effect of an accounting change, was $0.39 in fiscal 2003, decreased 45% from $0.71 per share reported in fiscal 2002. The weighted average common shares outstanding for purposes of computing diluted earnings per share in fiscal 2003 was 19,923,000 shares as compared to 20,059,000 shares last year.

The Company has completed the transitional goodwill impairment test required by Statement of Financial Accounting Standards No. 142 (SFAS No. 142), "Goodwill and Other Intangible Assets." This test required the Company, through an independent appraisal firm, to assess the fair value, as determined on a discounted cash flow basis, of each reporting unit that had goodwill on its balance sheet, and compare that value to the carrying value of the reporting unit's net assets as of July 1, 2002. The Company has determined for its fiscal 2003 transitional goodwill impairment test that it has eight reporting units, each of which represents an acquired business that currently operates in the organizational structure one level below the business segment level. Based upon phase one of the analysis, there was an indication that the recorded net goodwill of two reporting units in the Lighting Segment (totaling $23,593,000) and one reporting unit in the Graphics Segment (totaling $929,000) was significantly impaired. Upon completion of the second phase of the transitional goodwill impairment test, it was determined that the goodwill in all three reporting units was fully impaired. The impairment of $24,522,000 is a non-cash and non-operating charge. It has been booked in the amount of $18,541,000, net of income taxes, as a change in accounting methods and has been recorded as of the date of adoption of SFAS No. 142, July 1, 2002. The Company has determined that it will perform its annual goodwill impairment test in accordance with SFAS No. 142 as of July 1st each year.

The Company recorded a net loss of $10,748,000 in fiscal 2003 as compared to net income of $14,186,000 in fiscal 2002. The decrease is primarily the result of the $18,541,000 goodwill impairment loss that was recorded as an accounting change, and decreased income from business operations ($7,793,000 as compared to $14,186,000). Diluted earnings or (loss) per share was $(0.54) in fiscal 2003 as compared to $0.71 per share reported in fiscal 2002.

LIQUIDITY AND CAPITAL RESOURCES

The Company considers its level of cash on hand, its borrowing capacity, its 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 June 30, 2004 the Company had working capital of $64.7 million, compared to $59.6 million at June 30, 2003. The ratio of current assets to current liabilities decreased to 3.0 to 1 from 3.5 to 1. The $5.1 million increase in working capital is primarily attributed to increased accounts receivable, inventories and other current assets, partially offset by increased accounts payable and accrued expenses, and decreased refundable income taxes. The $5.2 million increase in accounts receivable is due to higher fourth quarter fiscal 2004 sales as compared to fourth quarter fiscal 2003, as well as an increase in days sales outstanding (DSO). The DSO was 59 days at June 30, 2004, up from 58 days at June 30, 2003. Inventories, primarily raw materials and finished goods, have increased $7.3 million in 2004. Raw materials and work in process are up an aggregate $4.1 million, and finished goods are up approximately $3.2 million since the end of fiscal 2003. Other current assets increased approximately $2.4 million related primarily to increased receivables ($1.8 million) related to a facilities expansion program in a state in which the Company operates, supplier volume rebates and a sales representative program, and a larger (increased by $0.6 million) net current deferred federal income tax asset at June 30, 2004.

The Company generated $12.1 million of cash from operating activities in fiscal 2004 as compared to $13.2 million in fiscal 2003. The $1.1 million decrease in net cash flows from operating activities in fiscal 2004 is primarily the net result of increased income before cumulative effect of accounting change ($0.9 million favorable), an increase in accounts receivable rather than a decrease (unfavorable change of $10.2 million), more of an increase in inventories (unfavorable change of $5.9 million), an aggregate $7.3 million increase in accounts payable and accrued expenses in fiscal 2004 as compared to an aggregate $5.8 million decrease last year (net $13.1 million favorable), and a more of a reduction in refundable income taxes (favorable change of $1.1 million).

Net accounts and notes receivables were $42.5 million and $37.3 million at June 30, 2004 and June 30, 2003, respectively. The 14% increase in receivables is due primarily to the 16% increase in fiscal 2004 last month net sales as compared to the same month last year. The Company converted one Graphics Segment customer account (petroleum/convenience store customer) into a collateralized note receivable during fiscal 2002. The balance of the note and unsecured receivable, net of reserves, was $0.6 million and $0.9 million, respectively, as of June 30, 2004 and 2003, down significantly from the $3.1 million total receivable balance from this customer as of June 30, 2002. The Company has three of this customer's retail sites as collateral on the note receivable. The Company is currently in litigation with this customer to obtain collection of all amounts owed to the Company. During the year, the Company carried a $0.2 million unsecured receivable from Kmart, a large national retailer that filed Chapter 11 bankruptcy in January 2002. This bankruptcy claim is not yet settled, however the Company believes it will finalize it at an amount in excess of the $0.2 million receivable. The Company provided $0.7 million bad debt expense in fiscal 2004 as compared to $1.5 million in fiscal 2003. The Company believes that its receivables are ultimately collectible or recoverable, net of certain reserves, and that aggregate allowances for doubtful accounts are adequate.

Inventories at June 30, 2004 are up $7.3 million from June 30, 2003. The inventory increase occurred in the Lighting Segment in support of shipping requirements of various lighting programs, primarily that of a large national retailer that began in the third quarter of fiscal 2004 and that is expected to continue for about two years. Also, increased raw material costs and labor rates contributed to higher inventories. The June 30, 2004 balance of trade accounts payable is reflective of the increase in inventories.

Cash generated from operations and borrowing capacity under its line of credit agreement are the Company's primary source of liquidity. In addition, the Company has an unsecured $50 million revolving line of credit with its bank group. As of August 20, 2004 there was approximately $33.9 million available on this line of credit. This line of credit is composed of a $30 million three year committed credit facility expiring in fiscal 2007 and a $20 million credit facility with an annual renewal in

the third quarter of fiscal 2005. The Company believes that the total of available lines of credit plus cash flows from operating activities is adequate for the Company's fiscal 2004 operational and capital expenditure needs. The Company is in compliance with all of its loan covenants.

Capital expenditures of $4.7 million in fiscal 2004 compare to $5.5 million in fiscal 2003. The primary spending early in fiscal 2003 was for final construction costs of the $11 million manufacturing facility for LSI Lightron. The Company commenced operations in this facility in July 2003. Fiscal 2004 spending is primarily for tooling and equipment (approximately $3.8 million), and capitalization of system design costs related to the Company's fully integrated enterprise resource planning/business operating system ($0.9 million). Total capital expenditures in fiscal 2005 are expected to be approximately $6 million, exclusive of business acquisitions.

The Company used $7.4 million in financing activities in fiscal 2004 as compared to a use of $7.9 million in fiscal 2003. The change between years is primarily the net result of increased dividend payments (unfavorable $1.4 million) pursuant to the Company's increased indicated annual dividend payment amount, partially offset by lower net payments on the Company's long-term debt in fiscal 2004 (favorable $1.4 million) and increased cash flow from the exercise of stock options (favorable $0.4 million).

The Company has been implementing a fully integrated enterprise resource planning/business operating system over the past several fiscal years, and will continue to do so throughout all operations of the Company, with completion of the implementation estimated for fiscal 2006. With the completion of software design for use throughout the Company as well as implementation of this software in the Company's largest lighting operations in Cincinnati and Kentucky, the approximate $9 million total software expenditures that have been capitalized to date are being depreciated in accordance with the American Institute of Certified Public Accountants' Statement of Position 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." The Company is depreciating this software over an eight year life from the date placed in service, with a total of $1.5 million of depreciation having been expensed to date. The Company expects to capitalize very little additional design costs for this internal-use software, and expects to expense implementation costs as they are incurred for the remaining operating business units.

As of June 30, 2004, the Company had the following contractual obligations pursuant to long-term borrowings, leases, purchase obligations not recognized in the financial statements (i.e., open purchase orders issued to suppliers), and all other liabilities reflected in the balance sheet (in thousands):

Contractual Obligations as of June 30, 2004	Payments due by period				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Long-Term Debt Obligations	$11,554	$ —	$11,554	$ —	$ —
Capital Lease Obligations	—	—	—	—	—
Operating Lease Obligations	5,205	1,515	2,594	1,096	—
Purchase Obligations	13,003	12,955	48	—	—
Other Long-Term Liabilities	—	—	—	—	—
Total	$29,762	$14,470	$14,196	$ 1,096	$ —

On August 11, 2004 the Board of Directors declared a regular quarterly cash dividend of $0.072 per share (approximately $1,422,000), payable September 14, 2004 to shareholders of record on September 7, 2004. During fiscal 2004, the Company paid cash dividends of $5,206,000, as compared to $3,784,000 in fiscal 2003. The declaration and amount of dividends will be determined by the Company's Board of Directors, in its discretion, based upon its evaluation of earnings, cash flow, capital requirements and future business developments and opportunities, including acquisitions.

Carefully selected acquisitions have long been an important part of the Company's strategic growth plans. The Company continues to seek out, screen and evaluate potential acquisitions that could add to the lighting or graphics product lines or enhance the Company's position in selected markets. The Company believes adequate financing for any such investments or acquisitions will be available through future borrowings or through the issuance of common or preferred shares in payment for acquired businesses.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company is required to make estimates and judgments in the preparation of its financial statements that affect the reported amounts of assets, liabilities, revenues and expenses, and related footnote disclosures. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. The Company continually reviews these estimates and their underlying assumptions to ensure they remain appropriate. The Company believes the items discussed below are among its most significant accounting policies because they utilize estimates about the effect of matters that are inherently uncertain and therefore are based on management's judgment. Significant changes in the estimates or assumptions related to any of the following critical accounting policies could possibly have a material impact on the financial statements.

Revenue Recognition

The Company recognizes revenue in accordance with Securities Exchange Commission Staff Accounting Bulletin No. 104, "Revenue Recognition." Revenue is recognized when title to goods and risk of loss have passed to the customer, there is persuasive evidence of a purchase arrangement, delivery has occurred or services have been rendered, and collectibility is reasonably assured. Revenue is typically recognized at time of shipment. Sales are recorded net of estimated returns, rebates and discounts. Any cash received from customers prior to the recognition of revenue is accounted for as a customer pre-payment and is included in accrued expenses.

The Company has four sources of revenue: revenue from product sales; revenue from the installation of product; service revenue generated from providing the integrated design, project and construction management, site engineering, and site permitting; and revenue from shipping and handling. *Product revenue* is recognized on product-only orders at the time of shipment. Product revenue related to orders where the customer requires the Company to install the product is generally recognized when the product is installed. In some situations, product revenue is recognized when the product is shipped, before it is installed, because by agreement the customer has taken title to and risk of ownership for the product before installation has been completed. Other than normal product warranties or the possibility of installation, the Company has no post-shipment responsibilities. *Installation revenue* is recognized when the products have been fully installed. The Company is not always responsible for installation of products it sells and has no post-installation service contracts or responsibilities. *Service revenue* from integrated design, project and construction management, site engineering and permitting is recognized at the completion of the contract with the customer. With larger customer contracts involving multiple sites, the customer may require progress billings for completion of identifiable, time-phased elements of the work, in which case revenue is recognized at the time of the progress billing. *Shipping and handling revenue* coincides with the recognition of revenue from sale of the product.

Asset Impairment

Carrying values of goodwill and other intangible assets with indefinite lives are reviewed at least annually for possible impairment in accordance with Statement of Financial Accounting Standards No. 142 (SFAS No. 142), "Goodwill and Other Intangible Assets," which was adopted on July 1, 2002. The Company's impairment review involves the estimation of the fair value of goodwill and indefinite-lived intangible assets using a discounted cash flow approach, at the reporting unit level, that 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 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 unexpected adverse business conditions, economic factors and unanticipated technological change or competitive activities may signal that an asset has become impaired. An impairment charge of $24.5 million, or $18.5 million net of tax, related to goodwill was recorded in fiscal 2003 as the cumulative effect of an accounting change and charged against income. See Note 5 to the financial statements for further discussion.

Carrying values for long-lived tangible assets and definite-lived intangible assets, excluding goodwill, are reviewed for possible impairment as circumstances warrant in connection with Statement of Financial Accounting Standards No. 144 (SFAS No. 144), "Accounting for the Impairment or Disposal of Long-Lived Assets," which was adopted on July 1, 2002. Impairment reviews are conducted at the judgment of Company management when it believes that a change in circumstances in the business or external factors warrants a review. Circumstances such as the discontinuation of a product or product line, a sudden or consistent decline in the forecast for a product, changes in technology or in the way an asset is being used, a history of operating or cash flow losses, or an adverse change in legal factors or in the business climate, among others, may trigger an impairment review. The Company's initial impairment review to determine if a potential impairment charge is required is based on an undiscounted cash flow analysis at the lowest level for which identifiable cash flows exist. The analysis requires judgment with respect to changes in technology, the continued success of product lines and future volume, revenue and expense growth rates, and discount rates. There were no impairment charges related to long-lived tangible assets or definite-lived intangible assets recorded by the Company during 2003 or 2004.

Credit and Collections

The Company maintains allowances for doubtful accounts receivable for estimated losses resulting from either customer disputes or the inability of its customers to make required payments. If the financial condition of the Company's customers were to deteriorate, resulting in their inability to make the required payments, the Company may be required to record additional allowances or charges against income. The Company determines its allowance for doubtful accounts by first considering all known collectibility problems of customers' accounts, and then applying certain percentages against the various aging categories of the remaining receivables. The resulting allowance for doubtful accounts receivable is an estimate based upon the Company's knowledge of its business and customer base, and historical trends. The Company also establishes allowances, at the time revenue is recognized, for returns and allowances, discounts, pricing and other possible customer deductions. These allowances are based upon historical trends.

NEW ACCOUNTING PRONOUNCEMENTS

In December 2003, the Securities and Exchange Commission released Staff Accounting Bulletin (SAB) 104, "Revenue Recognition." SAB 104 updates the guidance included in Topic 13 of the codification of staff accounting bulletins to make it consistent with current authorative accounting pronouncements. The Company's policy on Revenue Recognition is consistent with SAB 104.

LSI Industries Inc.

CONSOLIDATED BALANCE SHEETS

June 30, 2004 and 2003

(In thousands, except shares)

	2004	2003
ASSETS		
Current Assets		
Cash and cash equivalents	**$ 205**	$ 239
Accounts and notes receivable, less allowance for doubtful accounts of $1,264 and $959, respectively	**42,545**	37,314
Inventories	**47,672**	40,326
Refundable income taxes	**516**	1,823
Other current assets	**6,185**	3,803
Total current assets	**97,123**	83,505
Property, Plant and Equipment, at cost		
Land	**6,698**	6,692
Buildings	**32,120**	31,987
Machinery and equipment	**55,692**	47,716
Construction in progress	**209**	5,667
	94,719	92,062
Less accumulated depreciation	**(40,567)**	(37,053)
Net property, plant and equipment	**54,152**	55,009
Goodwill, net	**17,303**	17,303
Other Intangible Assets, net	**4,710**	5,193
Other Assets, net	**1,444**	1,766
	$174,732	$162,776

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

	2004	2003
LIABILITIES & SHAREHOLDERS' EQUITY		
Current Liabilities		
Current maturities of long-term debt	**$ —**	$ 85
Accounts payable	**18,289**	13,603
Accrued expenses	**14,110**	10,184
Total current liabilities	**32,399**	23,872
Long-Term Debt	**11,554**	13,999
Deferred Income Taxes	**1,333**	—
Other Long-Term Liabilities	**583**	—
Shareholders' Equity		
Preferred shares, without par value; Authorized 1,000,000 shares, none issued	**—**	—
Common shares, without par value; Authorized 30,000,000 shares; Outstanding 19,733,804 and 19,702,020 shares, respectively	**53,059**	52,585
Retained earnings	**75,804**	72,320
Total shareholders' equity	**128,863**	124,905
	$174,732	$162,776

CONSOLIDATED INCOME STATEMENTS

For the years ended June 30, 2004, 2003, and 2002
(In thousands, except per share)

	2004	2003	2002
Net sales	**$241,405**	$213,133	$259,261
Cost of products and services sold	**181,883**	157,966	186,838
Gross profit	**59,522**	55,167	72,423
Selling and administrative expenses	**45,488**	43,801	49,039
Operating income	**14,034**	11,366	23,384
Interest (income)	**(23)**	(259)	(51)
Interest expense	**260**	378	575
Income before income taxes	**13,797**	11,247	22,860
Income tax expense	**5,107**	3,454	8,674
Income before cumulative effect of accounting change	**8,690**	7,793	14,186
Cumulative effect of accounting change, net of tax	**—**	18,541	—
Net income (loss)	**$ 8,690**	$ (10,748)	$ 14,186
Earnings (loss) per common share			
Basic			
Earnings per share before cumulative effect of accounting change	**$ .44**	$ .40	$ .72
Earnings (loss) per share	**$ .44**	$ (.55)	$ .72
Diluted			
Earnings per share before cumulative effect of accounting change	**$ .43**	$ .39	$ .71
Earnings (loss) per share	**$ .43**	$ (.54)	$ .71

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

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

For the years ended June 30, 2004, 2003, and 2002
(In thousands, except per share)

	Common Shares			
	Number of Shares	Amount	Retained Earnings	Total
Balance at June 30, 2001	19,572	$50,808	$76,385	$127,193
Net income	—	—	14,186	14,186
Purchase of treasury shares	(16)	(256)	—	(256)
Deferred stock compensation	—	267	—	267
Stock options exercised, net	165	1,678	—	1,678
Dividends - $.192 per share	—	—	(3,719)	(3,719)
Balance at June 30, 2002	19,721	52,497	86,852	139,349
Net (loss)	—	—	(10,748)	(10,748)
Purchase of treasury shares	(30)	(243)	—	(243)
Deferred stock compensation	—	240	—	240
Stock options exercised, net	11	91	—	91
Dividends - $.192 per share	—	—	(3,784)	(3,784)
Balance at June 30, 2003	19,702	52,585	72,320	124,905
Net income	**—**	**—**	**8,690**	**8,690**
Purchase of treasury shares	**(19)**	**(211)**	**—**	**(211)**
Deferred stock compensation	**—**	**185**	**—**	**185**
Stock options exercised, net	**51**	**500**	**—**	**500**
Dividends - $.264 per share	**—**	**—**	**(5,206)**	**(5,206)**
Balance at June 30, 2004	**19,734**	**$53,059**	**$75,804**	**$128,863**

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

LSI Industries Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the years ended June 30, 2004, 2003, and 2002
(In thousands)

	2004	2003	2002
Cash Flows From Operating Activities			
Net income (loss)	**$ 8,690**	$(10,748)	$14,186
Non-cash items included in income			
Cumulative effect of accounting change, before taxes	**—**	24,522	—
Depreciation and amortization	**5,925**	5,702	6,096
Deferred income taxes	**1,179**	(4,365)	2,191
Deferred compensation plan	**185**	240	267
(Gain) loss on disposition of fixed assets	**116**	31	(4)
Change (excluding effects of acquisitions) in			
Accounts and notes receivable	**(5,231)**	4,959	9,336
Inventories	**(7,346)**	(1,480)	(3,767)
Refundable income taxes	**1,307**	166	(1,135)
Accounts payable	**4,686**	(1,307)	(358)
Accrued expenses and other	**2,603**	(4,502)	1,144
Net liabilities from discontinued operations	**—**	—	(711)
Net cash flows from operating activities	**12,114**	13,218	27,245
Cash Flows From Investing Activities			
Purchase of property, plant, and equipment	**(4,708)**	(5,452)	(16,846)
Proceeds from sale of fixed assets	**7**	21	7
Acquisition of businesses, net of cash received	**—**	—	(1,603)
Net cash flows from investing activities	**(4,701)**	(5,431)	(18,442)
Cash Flows From Financing Activities			
Increase (decrease) of borrowings under line of credit	**—**	—	(552)
Proceeds from issuance of long-term debt	**1,725**	3,746	—
Payment of long-term debt	**(4,255)**	(7,715)	(5,937)
Cash dividends paid	**(5,206)**	(3,784)	(3,719)
Exercise of stock options	**500**	91	1,678
Purchase of treasury shares	**(211)**	(243)	(256)
Net cash flows from financing activities	**(7,447)**	(7,905)	(8,786)
Increase (decrease) in cash and cash equivalents	**(34)**	(118)	17
Cash and cash equivalents at beginning of year	**239**	357	340
Cash and cash equivalents at end of year	**$ 205**	$ 239	$ 357

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidation:

The consolidated financial statements include the accounts of LSI Industries Inc. (an Ohio corporation) and its subsidiaries, all of which are wholly owned. All significant intercompany transactions and balances have been eliminated.

Revenue recognition:

The Company has four sources of revenue: revenue from product sales; revenue from the installation of product; service revenue generated from providing the integrated design, project and construction management, site engineering, and site permitting; and revenue from shipping and handling.

Product revenue is recognized on product-only orders at the time of shipment. Product revenue related to orders where the customer requires the Company to install the product is generally recognized when the product is installed. In some situations, product revenue is recognized when the product is shipped, before it is installed, because by agreement the customer has taken title to and risk of ownership for the product before installation has been completed. Other than normal product warranties or the possibility of installation, the Company has no post-shipment responsibilities.

Installation revenue is recognized when the products have been fully installed. The Company is not always responsible for installation of products it sells and has no post-installation service contracts or responsibilities.

Service revenue from integrated design, project and construction management, site engineering and permitting is recognized at the completion of the contract with the customer. With larger customer contracts involving multiple sites, the customer may require progress billings for completion of identifiable, time-phased elements of the work, in which case revenue is recognized at the time of the progress billing.

Shipping and handling revenue coincides with the recognition of revenue from sale of the product.

Amounts received from customers prior to the recognition of revenue are accounted for as customer pre-payments and are included in accrued expenses.

Credit and Collections:

The Company maintains allowances for doubtful accounts receivable for estimated losses resulting from either customer disputes or the inability of its customers to make required payments. If the financial condition of the Company's customers were to deteriorate, resulting in their inability to make the required payments, the Company may be required to record additional allowances or charges against income. The Company determines its allowance for doubtful accounts by first considering all known collectibility problems of customers' accounts, and then applying certain percentages against the various aging categories of the remaining receivables. The resulting allowance for doubtful accounts receivable is an estimate based upon the Company's knowledge of its business and customer base, and historical trends. The Company also establishes allowances, at the time revenue is recognized, for returns and allowances, discounts, pricing and other possible customer deductions. These allowances are based upon historical trends.

Cash and cash equivalents:

The cash balance includes cash and cash equivalents which have original maturities of less than three months. At June 30, 2004 and 2003 the bank balances included $916,000 and $1,937,000, respectively, in excess of FDIC insurance limits.

Inventories:

Inventories are stated at the lower of cost or market. Cost is determined on the first-in, first-out basis.

Property, plant and equipment and related depreciation:

Property, plant and equipment are stated at cost. Major additions and betterments are capitalized while maintenance and repairs are expensed. For financial reporting purposes, depreciation is computed on the straight-line method over the estimated useful lives of the assets as follows:

Buildings	31 – 40 years
Machinery and equipment	3 – 10 years
Computer software	3 – 8 years

Costs related to the purchase, internal development, and implementation of the Company's business operating software system are either capitalized or expensed in accordance with the American Institute of Certified Public Accountants' Statement of Position 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." The current business operating software was first implemented in January 2000. All costs capitalized for the business operating software are being depreciated over an eight year life from the date placed in service. Other purchased computer software is being depreciated over periods ranging from three to five years.

Intangible assets:

Intangible assets consisting of customer lists, trade names, patents and trademarks are recorded on the Company's balance sheet and are being amortized to expense over periods ranging between twelve and forty years. The excess of cost over fair value of assets acquired ("goodwill") was amortized to expense over periods ranging between fifteen and forty years through fiscal 2002. Beginning in fiscal 2003, goodwill is no longer amortized, but is subject to review for impairment. See additional information about goodwill and intangibles in Note 5. The Company periodically evaluates intangible assets, goodwill and other long-lived assets for permanent impairment. Impairments have been recorded only with respect to goodwill (see Note 5).

Fair value of financial instruments:

The Company has financial instruments consisting primarily of cash and cash equivalents, 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. The Company has no financial instruments with off-balance sheet risk.

Contingencies:

The Company is party to various negotiations, customer bankruptcies, and legal proceedings arising in the normal course of business. 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.

Employee benefit plans:

The Company has a defined contribution retirement plan and a discretionary profit sharing plan covering substantially all of its employees, a second discretionary profit sharing plan covering employees of one subsidiary, and a non-qualified deferred compensation plan covering certain employees. The costs of employee benefit plans are charged to expense and funded annually. Total costs were $1,755,000 in 2004, $1,500,000 in 2003, and $1,876,000 in 2002.

Income taxes:

Deferred income taxes are provided on items that are reported as either income or expense in different time periods for financial reporting purposes than they are for income tax purposes. Deferred income tax assets and liabilities are reported on the Company's balance sheet. See also Note 9.

Earnings per common share:

The computation of basic earnings per common share is based on the weighted average common shares outstanding for the period. The computation of diluted earnings per share is based on the weighted average common shares outstanding for the period and includes common share equivalents. Common share equivalents include the dilutive effect of stock options, contingently issuable shares (for which issuance has been determined to be probable), and common shares to be issued under a deferred compensation plan, all of which totaled 321,000 shares in 2004, 215,000 shares in 2003, and 415,000 shares in 2002. See also Note 3.

Stock options:

The company applies the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." Accordingly, no compensation expense has been reflected in the financial statements as the exercise price of options granted to employees and non-employee directors is equal to the fair market value of the Company's common shares on the date of grant. The Company has adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123 (SFAS No. 123), "Accounting for Stock Based Compensation."

If the Company had adopted the expense recognition provisions of SFAS No. 123, net income and earnings per share for the years ended June 30, 2004, 2003, and 2002 would have been as follows:

(In thousands except earnings per share)	**2004**	2003	2002
Net income (loss)			
As reported	**$ 8,690**	$(10,748)	$14,186
Stock option expense	**354**	409	534
Pro forma	**$ 8,336**	$(11,157)	$13,652
Earnings (loss) per common share			
Basic			
As reported	**$ 0.44**	$ (0.55)	$ 0.72
Pro forma	**$ 0.42**	$ (0.57)	$ 0.70
Diluted			
As reported	**$ 0.43**	$ (0.54)	$ 0.71
Pro forma	**$ 0.42**	$ (0.56)	$ 0.68

Since SFAS No. 123 has not been applied to options granted prior to December 15, 1994, the resulting compensation cost shown above may not be representative of that expected in future years.

Recent pronouncements:

In December 2003, the Securities and Exchange Commission released Staff Accounting Bulletin (SAB) 104, "Revenue Recognition." SAB 104 updates the guidance included in Topic 13 of the codification of staff accounting bulletins to make it consistent with current authorative accounting pronouncements. The Company's policy on Revenue Recognition is consistent with SAB 104.

Comprehensive income:

The Company does not have any comprehensive income items other than net income.

Reclassification:

Certain reclassifications may have been made to prior year amounts in order to be consistent with the presentation for the current year, including reclassification of gain or loss on sale of fixed assets from other (income) expense up to cost of products and services sold.

Use of estimates:

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires the Company to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

NOTE 2 - BUSINESS SEGMENT INFORMATION

Effective July 1, 2003, the Company re-aligned its business segments and now operates in the following two business segments: the Lighting Segment and the Graphics Segment. The Company is organized such that the chief operating decision maker (the President and Chief Executive Officer) now receives financial and operating information relative to these two business segments, and organizationally, has a President of LSI Lighting Solutions *Plus* and a President of LSI Graphics Solutions *Plus* reporting directly to him. In the seven years prior to fiscal 2004, the Company reported business segments as the Image Segment and the Commercial/Industrial Lighting Segment. All prior period information has been revised to reflect the Company's new segments. The Company's most significant market is the petroleum/convenience store market with approximately 28%, 29% and 34% of total net sales concentrated in this market in fiscal 2004, 2003, and 2002, respectively.

The Company considers its geographic areas to be: 1) the United States, and 2) foreign. The foreign content of business is represented by 3%, or less, of total net sales in fiscal years 2002 through 2004. All capital expenditures, depreciation and amortization, and identifiable assets are in the United States. The following information is provided for the following periods:

(In thousands)	**2004**	2003	2002
Net sales:			
Lighting Segment	**$159,748**	$136,076	$147,930
Graphics Segment	**81,657**	77,057	111,331
	$241,405	$213,133	$259,261
Operating income:			
Image Segment	**$ 8,848**	$ 7,558	$ 11,484
Graphics Segment	**5,186**	3,808	11,900
	$ 14,034	$ 11,366	$ 23,384
Identifiable assets:			
Lighting Segment	**$110,616**	$ 96,582	$108,538
Graphics Segment	**63,002**	63,437	79,129
	173,618	160,019	187,667
Corporate	**1,114**	2,757	2,175
	$174,732	$162,776	$189,842
Capital expenditures:			
Lighting Segment	**3,160**	$ 4,647	$ 14,096
Graphics Segment	**1,548**	805	2,750
	$ 4,708	$ 5,452	$ 16,846
Depreciation and amortization:			
Lighting Segment	**$ 4,252**	$ 3,836	$ 3,378
Graphics Segment	**1,673**	1,866	2,718
	$ 5,925	$ 5,702	$ 6,096

Operating income of the business segments includes net sales less all operating expenses, including allocations of corporate expense. Sales between business segments are immaterial.

Identifiable assets are those assets used by each segment in its operations, including allocations of shared assets. Corporate assets consist primarily of cash and cash equivalents, and refundable income taxes. The decrease in identifiable assets in fiscal 2003 is primarily related to the write-off of impaired goodwill pursuant to the Company's implementation of Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (see Note 5).

NOTE 3 - EARNINGS PER COMMON SHARE

The following table presents the amounts used to compute earnings per common share and the effect of dilutive potential common shares on net income and weighted average shares outstanding:

(In thousands, except per share)	**2004**	2003	2002
BASIC EARNINGS PER SHARE			
Income before continuing effect of accounting change	**$ 8,690**	$ 7,793	$14,186
Cumulative effect of accounting change	**—**	18,541	—
Net income (loss)	**$ 8,690**	$(10,748)	$14,186
Weighted average shares outstanding during the period, net of treasury shares	**19,717**	19,708	19,644
Basic earnings per share before cumulative effect of accounting change	**$ 0.44**	$ 0.39	$0.72
Cumulative effect of accounting change	**—**	(0.94)	—
Basic earnings (loss) per share	**$ 0.44**	$ (0.55)	$ 0.72

(In thousands, except per share)	**2004**	2003	2002
DILUTED EARNINGS PER SHARE			
Income before cumulative effect of accounting change	**$ 8,690**	$ 7,793	$14,186
Cumulative effect of accounting change	**—**	18,541	—
Net income (loss)	**$ 8,690**	$(10,748)	$14,186
Weighted average shares outstanding during the period, net of treasury shares	**19,717**	19,708	19,644
Effect of dilutive securities (A): Impact of common shares to be issued under stock option plans, a deferred compensation plan, and contingently issuable shares	**321**	215	415
Weighted average shares outstanding (B)	**20,038**	19,923	20,059
Diluted earnings per share before cumulative effect of accounting change	**$ 0.43**	$ 0.39	$ 0.71
Cumulative effect of accounting change	**—**	(0.93)	—
Diluted earnings (loss) per share	**$ 0.43**	$ (0.54)	$ 0.71

(A) 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.

(B) Options to purchase 248,160 common shares, 368,618 common shares and 2,578 common shares at June 30, 2004, 2003, and 2002, respectively, were not included in the computation of diluted earnings per share because the exercise price was greater than the average fair market value of the common shares.

NOTE 4 - BALANCE SHEET DATA

The following information is provided as of June 30:

(In thousands)	**2004**	2003
Inventories:		
Raw materials	**$25,352**	$18,981
Work-in-process	**5,007**	7,181
Finished goods	**17,313**	14,164
	$47,672	$40,326
Accrued Expenses:		
Compensation and benefits	**$ 8,042**	$ 5,232
Customer prepayments	**2,141**	885
Other accrued expenses	**3,927**	4,067
	$14,110	$10,184

NOTE 5 - GOODWILL AND OTHER INTANGIBLE ASSETS

The Company completed its transitional goodwill impairment test in fiscal 2003 as of July 1, 2002, its date of adoption of SFAS No. 142. The Company determined for the transitional goodwill impairment test that it had eight reporting units, each of which represented an acquired business that operated in the organizational structure one level below the business segment level. Based upon this analysis, there was full impairment of the recorded net goodwill of two reporting units in the Lighting Segment (totaling $23,593,000) and one reporting unit in the Graphics Segment (totaling $929,000). The impairment of $24,522,000, a non-cash and non-operating charge, was booked in the amount of $18,541,000, net of income taxes, as a change in accounting method and was recorded as of the date of adoption of SFAS No. 142, July 1, 2002. The fiscal 2004 SFAS No. 142 testing was completed in the first quarter of fiscal 2004. The Company determined that it had three reporting units, two of which represented acquired businesses and one of which was an aggregation of acquired businesses at the business segment level. Test results indicated there was no impairment of goodwill.

The following tables present information about the Company's goodwill and other intangible assets on the dates indicated.

(In thousands)	**As of June 30, 2004**		
	Carrying Amount	Accumulated Amortization	Net
Goodwill	**$19,712**	**$ 2,409**	**$17,303**
Other Intangible Assets	**$ 6,430**	**$ 1,720**	**$ 4,710**

	As of June 30, 2003		
	Carrying Amount	Accumulated Amortization	Net
Goodwill	$ 19,712	$ 2,409	$ 17,303
Other Intangible Assets	$ 6,450	$ 1,257	$ 5,193

	Amortization Expense		
Fiscal Year	Goodwill	Other Intangible Assets	Total
2004	**$ —**	**$ 483**	**$ 483**
2003	$ —	$ 486	$ 486
2002	$ 1,350	$ 487	$ 1,837

Changes in the carrying amount of goodwill for the years ended June 30, 2003 and 2004, by operating segment, are as follows:

(In thousands)	Lighting Segment	Graphics Segment	Total
Balance June 30, 2002	$ 23,914	$ 17,911	$ 41,825
Impairment losses	(23,593)	(929)	(24,522)
Balance June 30, 2003	321	16,982	17,303
Impairment losses	—	—	—
Balance June 30, 2004	$ 321	$ 16,982	$ 17,303

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

	June 30, 2004	
(In thousands)	Gross Carrying Amount	Accumulated Amortization
Amortized Intangible Assets		
Customer list	**$5,400**	**$1,613**
Trademarks	**920**	**82**
Patents	**110**	**25**
	$6,430	**$1,720**

	June 30, 2003	
(In thousands)	Gross Carrying Amount	Accumulated Amortization
Amortized Intangible Assets		
Customer list	$5,400	$1,162
Trademarks	920	59
Patents	110	18
Non-compete agreements	20	18
	$6,450	$1,257

Aggregate amortization expense for other intangible assets was $483,000 in fiscal 2004, $486,000 in fiscal 2003 and $487,000 in fiscal 2002.

The Company expects to record amortization expense of $480,000 related to other intangible assets in each of the next five years following 2004.

The following table presents the effect of the Company's adoption of Statement of Financial Accounting Standards No. 142 (Goodwill and Other Intangible Assets).

(In thousands, except per share)	**2004**	2003	2002
Reported income before cumulative effect of accounting change	**$8,690**	$7,793	$14,186
Add back: Goodwill amortization, net of tax	**—**	—	939
Adjusted income before cumulative effect of accounting change	**$8,690**	$7,793	$15,125
Basic Earnings Per Share:			
Reported basic earnings per share before cumulative effect of accounting change	**$ .44**	$ .39	$ .72
Goodwill amortization	**—**	—	.05
Adjusted basic earnings per share before cumulative effect of accounting change	**$ .44**	$ .39	$ .77
Diluted Earnings Per Share:			
Reported diluted earnings per share before cumulative effect of accounting change	**$ .43**	$ .39	$ .71
Goodwill amortization	**—**	—	.04
Adjusted diluted earnings per share before cumulative effect of accounting change	**$ .43**	$ .39	$ .75

NOTE 6 - REVOLVING LINES OF CREDIT AND LONG-TERM DEBT

The Company has an unsecured $50 million revolving line of credit with its bank group. As of June 30, 2004 the available portion of this line of credit was $38.9 million. A portion of this credit facility is a $20 million line of credit that expires in the third quarter of fiscal 2005. The remainder of the credit facility is a $30 million three year committed line of credit that expires in fiscal 2007. Annually in the third quarter, the credit facility is renewable with respect to adding an additional year of commitment to replace the year just ended. Interest on the revolving lines of credit is charged based upon an increment over the LIBOR rate as periodically determined, an increment over the Federal Funds 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 50 and 75 basis points depending upon the ratio of indebtedness to earnings before interest, taxes, depreciation and amortization (EBITDA). The increment over the Federal Funds borrowing rate, as periodically determined, fluctuates between 150 and 200 basis points, and the commitment fee on the unused balance of the $30 million committed portion of the line of credit fluctuates between 15 and 25 basis points based upon the same leverage ratio. At June 30, 2004 the average interest rate on borrowings under this revolving line of credit was 1.66%. Under terms of these agreements, the Company has agreed to a negative pledge of assets, to maintain minimum levels of profitability and net worth, and is subject to certain maximum levels of leverage. The Company's borrowings under its bank credit facilities during fiscal year 2004 averaged approximately $11.0 million at an approximate average borrowing rate of 1.69%.

(In thousands)	**2004**	2003
Long-term debt:		
Revolving Line of Credit (3 year committed line)	**$11,554**	$13,384
Industrial Revenue Development Bond	**—**	700
	11,554	14,084
Less current maturities of long-term debt	**—**	85
Long-term debt	**$11,554**	$13,999

Future maturities of long-term debt at June 30, 2004 are as follows (in thousands):

2005	2006	2007	2008	2009	2010 and after
$—	$—	$11,554	$—	$—	$—

NOTE 7 - SHAREHOLDERS' EQUITY

The common shares of the Company were split 3-for-2 effective November 21, 2001, and were split 5-for-4 effective November 14, 2003. Accordingly, all share and per share data for all prior reporting periods have been restated to reflect these splits.

The Company has an equity compensation plan that covers all of its full-time employees and non-employee directors. The equity compensation replaced two stock option plans that still have outstanding options that may be exercised in the future. The options granted pursuant to this plan are granted at fair market value at date of grant. Options granted to non-employee directors are immediately exercisable and options granted to employees generally become exercisable 25% per year (cumulative) beginning one year after the date of grant. The number of shares reserved for issuance is 2,910,188, of which 2,242,843 shares were available for future grant as of June 30, 2004. The plan allows for the grant of incentive stock options, non-qualified stock options, stock appreciation rights, restricted and unrestricted stock awards, performance stock awards, and other stock awards.

Statement of Financial Accounting Standards No. 123 (SFAS No. 123) requires, at a minimum, pro forma disclosures of expense for stock-based awards based on their fair values. The fair value of each option on the date of grant has been estimated using the Black-Scholes option pricing model. The following weighted average assumptions were used for grants in fiscal 2004, 2003, and 2002.

	2004	2003	2002
Dividend yield	**2.16%**	1.89%	1.38%
Expected volatility	**47%**	48%	35%
Risk-free interest rate	**3.26%**	2.93%	2.16%–3.62%
Expected life	**4–9 yrs.**	8 yrs.	3–7 yrs.

The 7,550 options granted during fiscal 2004 to employees and non-employee directors had, at June 30, 2004, exercise prices ranging from $9.60 to $12.99, fair values ranging from $3.33 to $5.40 per option, and remaining contractual lives of four to nine years. At June 30, 2003, the 5,625 options granted during fiscal 2003 to non-employee directors had, at June 30, 2003, exercise prices of $8.59, fair values of $4.01 and remaining contractual lives of about nine years. The 252,298 options granted during fiscal 2002 to employees and non-employee directors had, at June 30, 2002, exercise prices ranging from $11.68 to $15.84, fair values ranging from $2.39 to $5.10 per option, and remaining contractual lives of four to nine years.

Information involving the stock option plans for the years ended June 30, 2004, 2003, and 2002 is shown in the table below:

	2004	
(Shares in thousands)	Shares	Weighted Average Exercise Price
Outstanding at beginning of year	**734**	**$ 9.74**
Granted	**7**	**$11.73**
Terminated	**(23)**	**$11.68**
Exercised	**(51)**	**$ 9.35**
Outstanding at end of year	**667**	**$ 9.73**
Exercisable at end of year	**487**	**$ 9.44**

	2003	
(Shares in thousands)	Shares	Weighted Average Exercise Price
Outstanding at beginning of year	805	$ 9.78
Granted	5	$ 8.76
Terminated	(65)	$10.46
Exercised	(11)	$ 8.13
Outstanding at end of year	734	$ 9.74
Exercisable at end of year	401	$ 9.27

	2002	
(Shares in thousands)	Shares	Weighted Average Exercise Price
Outstanding at beginning of year	756	$ 8.74
Granted	252	$11.82
Terminated	(36)	$ 9.08
Exercised	(167)	$ 8.24
Outstanding at end of year	805	$ 9.78
Exercisable at end of year	231	$ 9.27

The Company has a non-qualified deferred compensation plan providing for both Company contributions and participant deferrals of compensation. All Plan investments are in common shares of the Company. As of June 30, 2004 there were 37 participants with either partially or fully vested account balances. A total of 204,492 and 185,704 common shares were held in the Plan as of June 30, 2004 and 2003, respectively, and, accordingly, have been recorded as treasury shares.

On August 11, 2004, the Board of Directors declared a cash dividend of $0.072 per share to be paid September 14, 2004 to shareholders of record on September 7, 2004. Annual cash dividend payments made during fiscal years 2004, 2003, and 2002 were $0.264, $0.192, and $0.192 per share, respectively.

NOTE 8 - LEASES AND PURCHASE COMMITMENTS

The Company leases certain of its facilities and equipment under operating lease arrangements. Rental expense was $1,920,000 in 2004, $1,906,000 in 2003, and $1,875,000 in 2002. Minimum annual rental commitments under non-cancelable operating leases are: $1,515,000 in 2005, $1,419,000 in 2006, $1,175,000 in 2007, $939,000 in 2008, and $157,000 in 2009. There are no commitments beyond 2009. Purchase commitments of the Company totaled $13,003,000 as of June 30, 2004.

NOTE 9 - INCOME TAXES

The following information is provided for the years ended June 30:

(In thousands)	**2004**	2003	2002
Provision (benefit) for income taxes:			
Current federal	**$3,383**	$1,585	$5,633
Current state and local	**643**	253	850
Deferred	**1,081**	1,616	2,191
	$5,107	$3,454	$8,674
Reconciliation to federal statutory rate:			
Federal statutory tax rate	**34.1%**	34.0%	35.0%
State and local taxes, net of federal benefit	**3.3**	1.6	2.8
Federal and state tax credits	**(.8)**	(5.1)	—
Goodwill and other	**.4**	.2	.1
Effective tax rate	**37.0%**	30.7%	37.9%

The components of deferred income tax assets and (liabilities) at June 30, 2004 and 2003 are as follows:

(In thousands)	**2004**	2003
Reserves against current assets	**$ 883**	$ 778
Prepaid expenses	**(78)**	(687)
Accrued expenses	**794**	873
Depreciation	**(8,074)**	(6,330)
Goodwill and acquisition costs	**5,981**	6,117
Deferred compensation	**760**	694
Income tax credits	**917**	—
Valuation reserve	**(917)**	—
Net deferred income tax asset	**$ 266**	$1,445

Reconciliation to the balance sheets as of June 30, 2004 and 2003:

(In thousands)	**2004**	2003
Deferred income tax asset (liability) included in:		
Other current assets	**$1,599**	$ 964
Other assets	**—**	481
Long-term deferred income tax liability	**(1,333)**	—
Net deferred income tax asset (liability)	**$ 266**	$1,445

As of June 30, 2004 and 2003, the Company has recorded refundable income taxes as a current asset in the amounts of $516,000 and $1,823,000 respectively. The majority of the refundable income taxes relate to excess quarterly estimated federal income tax payments made during the year. Such refundable income taxes are applied in the subsequent fiscal year to the Company's quarterly estimated federal income tax payments. As of June 30, 2004 the Company has also recorded $11 million of state net operating loss carryforwards.

NOTE 10 - SUPPLEMENTAL CASH FLOW INFORMATION

(In thousands)	**2004**	2003	2002
Cash payments:			
Interest	**$ 248**	$ 367	$ 714
Income taxes	**$2,360**	$2,232	$8,003
Details of acquisitions:			
Cash paid for acquisitions	**$ —**	$ —	$1,603

NOTE 11 - SUMMARY OF QUARTERLY RESULTS (UNAUDITED)

(In thousands, except per share data)	Quarter Ended Sept. 30	Dec. 31	March 31	June 30	Fiscal Year
2004					
Net sales	$59,099	$64,116	$51,500	$66,690	$241,405
Gross profit	15,223	18,231	11,810	14,258 (a)	59,522
Income from continuing operations	4,204	6,399	1,477	1,954	14,034
Net income	2,601	4,006	920	1,163	8,690
Earnings per share					
Basic	$ .13	$ .20	$ .05	$ .06	$ .44
Diluted	$ .13	$ .20	$ .05	$ .06	$ .43 (b)
Range of share prices					
High	$ 11.95	$ 13.63	$ 14.79	$ 13.03	$ 14.79
Low	$ 8.40	$ 10.19	$ 11.15	$ 9.00	$ 8.40
2003					
Net sales	$56,045	$57,275	$44,228	$55,585	$213,133
Gross profit	15,054	15,020	10,562	14,531	55,167
Income from continuing operations before cumulative effect of accounting change	2,215	2,687	468	2,423	7,793
Net income (loss)	(16,326)(c)	2,687	468	2,423	(10,748)(c)
Earnings per share from continuing operations before cumulative effect of accounting change					
Basic	$ .11	$ .14	$ .02	$ .12	$ .39
Diluted	$ .11	$ .14	$ .02	$ .12	$ .39
Earnings (loss) per share					
Basic	$ (.83)	$ .14	$ .02	$ .12	$ (.55)
Diluted	$ (.82)	$ .14	$ .02	$ .12	$ (.54)
Range of share prices					
High	$ 14.83	$ 11.60	$ 11.29	$ 10.91	$ 14.83
Low	$ 7.12	$ 7.15	$ 6.59	$ 6.88	$ 6.59
2002					
Net sales	$67,049	$76,694	$58,261	$57,257	$259,261
Gross profit	19,084	21,740	15,897	15,702	72,423
Net income	3,702	4,607	2,549	3,328	14,186
Earnings per share					
Basic	$ .19	$ .23	$ .13	$ .17	$ .72
Diluted	$ .18	$ .23	$ .13	$ .17	$ .71
Range of share prices					
High	$ 14.74	$ 14.60	$ 17.91	$ 16.64	$ 17.91
Low	$ 10.38	$ 11.30	$ 13.04	$ 11.44	$ 10.38

(a) The fourth quarter of fiscal 2004 includes $1,086,000 of net unfavorable inventory adjustments in the Lighting Segment.
(b) The total of the earnings per share for each of the four quarters does not equal the total earnings per share for the full year because the calculations are based on the average shares outstanding during each of the individual periods.
(c) See Note 5 for discussion of an accounting change related to goodwill impairment.

At August 16, 2004, there were 392 shareholders of record. The Company believes this represents approximately 3,000 beneficial shareholders.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and
Shareholders of LSI Industries Inc.

We have audited the accompanying consolidated balance sheets of LSI Industries Inc. (an Ohio Corporation) and subsidiaries as of June 30, 2004 and 2003, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended June 30, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of LSI Industries Inc. and subsidiaries as of June 30, 2004 and 2003, and the results of their operations and their cash flows for the each of the three years in the period ended June 30, 2004, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 5 to the Consolidated Financial Statements, the Company adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," on July 1, 2002.

Cincinnati, Ohio
August 12, 2004

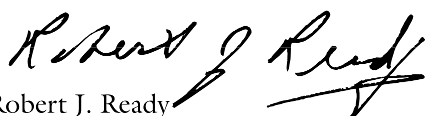
REPORT OF MANAGEMENT

The Management of LSI Industries Inc. is responsible for the preparation and accuracy of the financial statements and other information included in this report. The financial statements have been prepared in accordance with generally accepted accounting principles using, where appropriate, management's best estimates and judgment.

In meeting its responsibility for the reliability of the financial statements, the Company depends upon its system of internal accounting controls. The system is designed to provide reasonable assurance that assets are safeguarded and that transactions are properly authorized and recorded. The system is supported by policies and guidelines, and by careful selection and training of financial management personnel. The Company also has a Disclosure Controls Committee, whose responsibility is to help ensure appropriate disclosures and presentation of the financial statements and notes thereto. Additionally, the Company has an Internal Audit Department to assist in monitoring compliance with financial policies and procedures.

The Company's independent registered public accounting firm, Grant Thornton LLP, is retained to audit the LSI Industries Inc. consolidated financial statements. Their audit is conducted in accordance with generally accepted auditing standards and provides an independent assessment of the presentation of the Company's financial statements.

The Board of Directors meets its responsibility for overview of the Company's financial statements through its Audit Committee which is composed entirely of independent Directors who are not employees of the Company. The Audit Committee meets periodically with Management and with the independent registered public accounting firm to review and assess the activities of each in meeting their respective responsibilities. The independent registered public accounting firm has full access to the Audit Committee to discuss the results of their audit work, the adequacy of internal accounting controls, and the quality of financial reporting.



Robert J. Ready
President and Chief Executive Officer

Ronald S. Stowell
Vice President, Chief Financial Officer, and Treasurer

SELECTED FINANCIAL DATA

The following data has been selected from the Consolidated Financial Statements of the Company for the periods and dates indicated:

Income Statement Data:

(In thousands except per share)	**2004**	2003	2002	2001	2000
Net sales	**$241,405**	$213,133	$259,261	$233,940	$239,982
Cost of products sold	**181,883**	157,966	186,838	168,471	166,222
Operating expenses	**45,488**	43,801	49,039	48,175	45,219
Operating income	**14,034**	11,366	23,384	17,294	28,541
Interest (income)	**(23)**	(259)	(51)	(630)	(1,057)
Interest expense	**260**	378	575	607	189
Income from continuing operations before income taxes	**13,797**	11,247	22,860	17,317	29,409
Income taxes	**5,107**	3,454	8,674	6,716	11,130
Income from continuing operations before cumulative effect of accounting change and discontinued operations	**8,690**	7,793	14,186	10,601	18,279
Cumulative effect of accounting change, net of tax (a)	**—**	18,541	—	—	—
Discontinued operations	**—**	—	—	723	1,000
Net income (loss)	**$ 8,690**	$ (10,748)	$ 14,186	$ 9,878	$ 17,279
Earnings per common share from continuing operations before cumulative effect of accounting change					
Basic	**$ .44**	$ .39	$ .72	$ .55	$ .96
Diluted	**$ .43**	$ .39	$ .71	$ .54	$ .94
Earnings (loss) per common share					
Basic	**$ .44**	$ (.55)	$ .72	$ .51	$ .90
Diluted	**$ .43**	$ (.54)	$ .71	$ .50	$ .89
Cash dividends paid per share	**$ .26**	$ .19	$ .19	$ .21	$ .21
Weighted average common shares					
Basic	**19,717**	19,708	19,644	19,421	19,116
Diluted	**20,038**	19,923	20,059	19,731	19,414

Balance Sheet Data:

(At June 30)	**2004**	2003	2002	2001	2000
Working capital	**$ 64,724**	$ 59,633	$ 55,793	$ 62,119	$ 61,139
Total assets	**174,732**	162,776	189,842	181,759	146,783
Long-term debt, including current maturities	**11,554**	14,084	18,053	23,990	1,701
Shareholders' equity	**128,863**	124,905	139,349	127,193	118,212

(a) See Footnote No. 5 to the financial statements.

CORPORATE INFORMATION

Independent Registered Public Accounting Firm

Grant Thornton LLP
Cincinnati, Ohio

Legal Counsel

Keating, Muething & Klekamp, P.L.L.
Cincinnati, Ohio

Transfer Agent and Registrar

Computershare Investor Services, LLC
2 North LaSalle Street
Chicago, Illinois 60602

Dividend Reinvestment Plan

The LSI Industries Automatic Dividend Reinvestment and Stock Purchase Plan offers registered shareholders and employees an opportunity to purchase additional shares through automatic dividend reinvestment and/or optional cash investments. For additional information, contact:

Computershare Trust Co., Inc.
2 North LaSalle Street
Chicago, Illinois 60602
(866) 770-0656
E-mail: web.queries@computershare.com
Internet: www.computershare.com

Annual Meeting

The LSI Industries Inc. annual shareholders' meeting will be held Thursday, November 18, 2004 at 10:00 a.m. at the Company's corporate offices located at 10000 Alliance Road, Cincinnati, Ohio.

Form 10-K

Shareholders may obtain the 2004 Annual Report on Form 10-K as filed with the Securities and Exchange Commission without charge by writing to:

Investor Relations Manager
LSI Industries Inc.
10000 Alliance Road
Cincinnati, Ohio 45242

Market for the Company's Common Shares

LSI Industries Inc. Common Shares are traded on The Nasdaq Stock Market under the symbol LYTS.

Internet Site

The LSI Industries site on the Internet, *www.lsi-industries.com*, contains the Company's 10-K and 10-Q filings, proxy statements, other SEC filings, annual reports, news releases, stock prices, and a variety of other information about LSI Industries and its products and services.

OPERATING FACILITIES

Location		Telephone Number	Operations/Products & Services
Lighting Segment			
Ohio	Cincinnati	513-793-3200	Lighting
California	Fontana	909-357-0725	Distribution Center
Kansas	Kansas City	913-281-1100	Lighting
Kentucky	Independence	859-342-9944	Metal Fabrication
New York	New Windsor	845-220-3200	Lighting
Tennessee	Manchester	931-723-4442	Electrical Wire Harnesses
Texas	Dallas	972-466-1133	Lighting
Graphics Segment			
Ohio	North Canton	330-494-9444	Graphics; Engineering Services
	Cincinnati	513-793-3200	Menu Boards
Georgia	Atlanta	678-297-0972	Engineering Services
Kentucky	Independence	859-342-9944	Menu Boards
North Carolina	Charlotte	704-588-3850	Engineering Services
Oregon	Portland	503-892-2346	Engineering Services
Rhode Island	Woonsocket	401-766-7446	Graphics
Texas	Houston	713-744-4100	Graphics
Washington	Seattle	206-654-7045	Engineering Services

Seated (left to right): Dennis B. Meyer, Wilfred T. O'Gara, Gary P. Kreider; Standing (left to right): Robert J. Ready, James P. Sferra, Ronald S. Stowell

BOARD OF DIRECTORS

Robert J. Ready
President, Chief Executive Officer &
Chairman of the Board
Chairman of Executive Committee

James P. Sferra
Secretary - LSI Industries Inc.
Executive Vice President - Manufacturing
Member of Executive Committee

Gary P. Kreider
Senior Partner of Keating, Muething & Klekamp, P.L.L.
Cincinnati, Ohio
Member of Compensation Committee
Member of Nominating Committee

Dennis B. Meyer
Director of Midmark Corporation, Versailles, Ohio
Member of Audit Committee
Chairman of Compensation Committee
Member of Nominating Committee

Wilfred T. O'Gara
Chief Executive Officer – The O'Gara Group, Inc.
Cincinnati, Ohio
Chairman of Audit Committee
Member of Compensation Committee
Chairman of Nominating Committee

Mark A. Serrianne
Chief Executive Officer - Northlich, Inc.
Member of Audit Committee
Member of Compensation Committee
Member of Nominating Committee

CORPORATE OFFICERS AND EXECUTIVE MANAGEMENT

Robert J. Ready
President and Chief Executive Officer

James P. Sferra
Secretary; Executive Vice President - Manufacturing

Ronald S. Stowell
Vice President, Chief Financial Officer, and Treasurer

David W. McCauley
President LSI Graphic Solutions Plus

Scott D. Ready
President LSI Lighting Solutions Plus

LSI Industries Inc.
10000 Alliance Road
Cincinnati, Ohio 45242
(513) 793-3200 • FAX (513) 791-0813
www.lsi-industries.com