

Edgar Filing: DGSE COMPANIES INC - Form 10QSB

DGSE COMPANIES INC
Form 10QSB
August 16, 2004

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-QSB

(Mark One)

(X) Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended June 30, 2004

() Transition Report under Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from _____ to _____

Commission File Number 1-11048

DGSE Companies, Inc.

(Name of small business issuer)

Nevada

(State or other jurisdiction of incorporation or organization)

88-0097334

(I.R.S. Employer Identification Number)

2817 Forest Lane, Dallas, Texas

(Address of principal executive offices)

75234

(Zip Code)

(Issuer's telephone number, including area code) (972) 484-3662

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at July 30, 2004
-----	-----
Common Stock, \$.01 per value	4,913,290

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements

DGSE Companies, Inc. and Subsidiaries

CONSOLIDATED BALANCE SHEETS

(Unaudited)

ASSETS	June 30, 2004	December 31, 2003
	-----	-----
CURRENT ASSETS		
Cash and cash equivalents	\$ 319,157	735,293
Trade receivables	671,002	774,586
Other receivables	204,430	204,430
Inventories	6,982,645	6,673,865
Prepaid expenses	179,049	149,277
	-----	-----
Total current assets	8,356,283	8,537,451
MARKETABLE SECURITIES - AVAILABLE FOR SALE	263,799	243,446
PROPERTY AND EQUIPMENT - AT COST, NET	999,088	989,966
GOODWILL	1,151,120	1,151,120
OTHER ASSETS	149,809	149,546
	-----	-----
	\$ 10,920,099	\$ 11,071,529
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Notes payable	\$ 2,741,758	\$ 541,546
Current maturities of long-term debt	197,315	197,315
Accounts payable - trade	323,678	859,269
Accrued expenses	304,429	705,756
Customer deposits	78,105	150,088
Federal income taxes payable	360,568	512,991
	-----	-----
Total current liabilities	4,005,853	2,966,965
Long-term debt, less current maturities	1,222,336	2,719,482
Deferred income taxes	29,663	22,743
	-----	-----
Total liabilities	5,257,852	5,709,190
SHAREHOLDERS' EQUITY		
Common stock, \$.01 par value; authorized 10,000,000 shares; issued and outstanding 4,913,290 shares at June 30, 2004 and December 31, 2003	49,133	49,133
Additional paid-in capital	5,708,760	5,708,760
Accumulated other comprehensive income	13,433	--
Retained earnings (deficit)	(109,079)	(395,554)
	-----	-----
Total shareholders' equity	5,662,247	5,362,339

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=====	=====
\$ 10,920,099	\$ 11,071,529
=====	=====

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

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DGSE Companies, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF OPERATIONS
Three months ended
(Unaudited)

	June 30, 2004	June 30, 2003
Revenue		
Sales	\$ 6,170,192	\$ 5,671,014
Pawn services charges	47,084	41,630
	-----	-----
	6,217,276	5,712,644
Costs and expenses		
Cost of goods sold	4,988,111	4,594,741
Selling, general and administrative expenses	896,500	877,788
Depreciation and amortization	37,112	39,330
	-----	-----
	5,921,723	5,511,859
Operating income	295,553	200,785
	-----	-----
Other income (expense)		
Interest expense	(73,005)	(73,005)
	-----	-----
Total other income (expense)	(73,005)	(73,005)
Income (loss) before income taxes	222,548	127,780
Income tax expense	75,666	43,753
	-----	-----
Net income (loss) from continuing operations	146,882	84,027
Loss from discontinued operations, net of income taxes	(46,106)	(24,444)
	-----	-----
Net income (loss)	\$ 100,776	\$ 59,583
	=====	=====
Earnings per common share		
Basic and diluted		
From continuing operations	\$.03	\$.02
From discontinued operations	(.01)	(.01)
	-----	-----

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	\$.02	\$.01
	=====		=====	
Weighted average number of common shares:				
Basic		4,913,290		4,913,290
Diluted		5,161,616		4,913,290

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

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DGSE Companies, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF OPERATIONS
Six months ended
(Unaudited)

	June 30, 2004	June 30, 2003
	-----	-----
Revenue		
Sales	\$ 12,921,644	\$ 10,771,966
Pawn services charges	94,714	83,512
	-----	-----
	13,016,358	10,855,478
Costs and expenses		
Cost of goods sold	10,441,033	8,744,288
Selling, general and administrative expenses	1,805,482	1,738,174
Depreciation and amortization	72,397	85,098
	-----	-----
	12,318,912	10,567,560
Operating income	-----	-----
	697,446	287,918
Other income (expense)		
Interest expense	(145,058)	(141,035)
	-----	-----
Total other income (expense)	(145,058)	(141,035)
Income before income taxes	552,388	146,883
Income tax expense	187,812	49,940
	-----	-----
Net income from continuing operations	364,576	96,943
Loss from discontinued operations, net of income taxes	(78,101)	(58,803)
	-----	-----
Net income	\$ 286,475	\$ 38,140
	=====	=====

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Earnings per common share

Basic and diluted

From continuing operations	\$.07	\$.02
From discontinued operations	(.01)	(.01)
	-----	-----
	\$.06	\$.01
	=====	=====

Weighted average number of common shares:

Basic	4,913,290	4,913,290
Diluted	5,161,616	4,913,290

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

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DGSE COMPANIES, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six Months Ended June 30,	
	2004	2003
	-----	-----
Cash Flows From Operations		
Reconciliation of net loss to net cash used in operating activities		
Net income (loss)	\$ 286,475	\$ 38,140
Depreciation and amortization	72,397	85,098
(Increase) decrease in operating assets and liabilities		
Trade receivables	103,584	161,093
Inventories	(308,780)	(283,493)
Prepaid expenses and other current assets	(29,772)	(60,920)
Accounts payable and accrued expenses	(936,918)	(606,567)
Federal income taxes payable	(152,423)	(130,352)
Other assets	(263)	(5,267)
	-----	-----
Total net cash used in operating activities	(965,700)	(802,268)
Cash flows from investing activities		
Purchase of property and equipment	(81,519)	(10,100)
Change in customer deposits	(71,983)	(8,570)
	-----	-----
Net cash (used) provided by investing activities	(153,502)	(18,670)
Cash flows from financing activities		
Proceeds from notes issued	825,000	725,000
Payments on notes payable	(121,934)	(266,325)
	-----	-----
Net cash provided by financing activities	703,066	458,675
	-----	-----

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Net decrease in cash and cash equivalents	(416,136)	(362,263)
Cash and cash equivalents at beginning of year	735,293	498,408
	-----	-----
Cash and cash equivalents at end of period	\$ 319,157	\$ 136,145
	=====	=====

Supplemental disclosures:

Interest paid for the six months ended June 30, 2004 and 2003 was \$ 145,058 and \$ 141,035, respectively.

Income taxes paid for the six months ended June 30, 2004 and 2003 was \$300,000 and \$150,000, respectively.

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Basis of Presentation:

The accompanying unaudited condensed consolidated financial statements of DGSE Companies, Inc. and Subsidiaries include the financial statements of DGSE Companies, Inc. and its wholly-owned subsidiaries, DGSE Corporation, National Jewelry Exchange, Inc., Silverman Consultants, Inc. and Charleston Gold and Diamond Exchange, Inc. In July 2004 the Company sold the goodwill and trade name of Silverman Consultants, Inc. and discontinued the operations of this subsidiary. As a result, operating results for this subsidiary have been reclassified to discontinued operations for all periods presented. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included.

The Company's operating results for the three months ended March 31, 2004, are not necessarily indicative of the results that may be expected for the year ended December 31, 2004. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-KSB for the year ended December 31, 2003. Certain reclassifications were made to the prior year's consolidated financial statements to conform to the current year presentation.

(2) - Earnings per share

No schedule provided for the periods ended June 30, 2004 and 2003 because the effect on earnings per share is not dilutive.

(3) - Business segment information

The Company's operations by business segment for the three months ended June 30,

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were as follows:

	Jewelry	Discontinued Operations	Corporate & Other	Consolidated
	-----	-----	-----	-----
Revenues				
2004	\$ 6,217,276	\$ --	\$ --	\$ 6,217,276
2003	\$ 5,712,644	\$ --	\$ --	\$ 5,712,644
Net income (loss)				
2004	\$ 169,351	\$ (46,106)	\$ (22,469)	\$ 100,776
2003	\$ 95,790	\$ (24,444)	\$ (11,763)	\$ 59,583
Identifiable assets				
2004	\$ 9,991,161	\$ 414,694	\$ 514,244	\$ 10,920,099
2003	\$ 9,498,916	\$ 485,942	\$ 220,442	\$ 10,205,300
Capital expenditures				
2004	\$ 77,355	\$ --	\$ --	\$ 77,355
2003	\$ 7,707	\$ --	\$ --	\$ 7,707
Depreciation and amortization				
2004	\$ 35,237	\$ --	\$ 1,875	\$ 37,112
2003	\$ 37,455	\$ --	\$ 1,875	\$ 39,330

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The Company's operations by business segment for the six months ended June 30, were as follows:

	Jewelry	Discontinued Operations	Corporate & Other	Consolidated
	-----	-----	-----	-----
Revenues				
2004	\$ 13,016,358	\$ --	\$ --	\$ 13,016,358
2003	\$ 10,855,478	\$ --	\$ --	\$ 10,855,478
Net income (loss)				
2004	\$ 407,080	\$ (78,101)	\$ (42,504)	\$ 286,475
2003	\$ 104,455	\$ (58,803)	\$ (35,301)	\$ 38,140
Identifiable assets				
2004	\$ 9,991,161	\$ 414,694	\$ 514,244	\$ 10,920,099
2003	\$ 9,498,916	\$ 485,942	\$ 220,442	\$ 10,205,300
Capital expenditures				
2004	\$ 81,519	\$ --	\$ --	\$ 81,519
2003	\$ 10,100	\$ --	\$ --	\$ 10,100
Depreciation and				

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amortization						
2004	\$	68,647	\$	--	\$	72,397
2003	\$	81,348	\$	--	\$	85,098

(4) Other Comprehensive income:

Other comprehensive income is as follows:

	Before Tax Amount	Tax (Expense) Benefit	Net-of-Tax Amount
	-----	-----	-----
Other comprehensive income at December 31, 2003	\$ --	\$ --	\$ --
Unrealized holding gains arising during the Three months ended March 31, 2004	106,373	(36,167)	70,206
	-----	-----	-----
Other comprehensive income at March 31, 2004	106,373	(36,167)	70,206
Unrealized holding losses during the Three months ended June 30, 2004	(86,020)	29,247	(56,773)
	-----	-----	-----
Other comprehensive income at June 30, 2004	\$ 20,353	\$ (6,920)	\$ 13,433
	=====	=====	=====
Other comprehensive income loss at December 31, 2002	\$ (1,728,130)	\$ 593,180	\$ (1,134,950)
Unrealized holding gains arising during the Three months ended March 31, 2003	75,278	(25,594)	49,684
	-----	-----	-----
Other comprehensive income (loss) at March 31, 2003	(1,652,852)	567,586	(1,085,266)
Unrealized holding losses during the Three months ended June 30, 2003	(46,260)	15,728	(30,532)
	-----	-----	-----
Other comprehensive loss at June 30, 2003	\$ (1,699,112)	\$ 583,314	\$ (1,115,798)
	=====	=====	=====

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(5) Stock-based Compensation:

The Company accounts for stock-based compensation to employees using the intrinsic value method. Accordingly, compensation cost for stock options to employees is measured as the excess, if any, of the quoted market price of the Company's common stock at the date of the grant over the amount an employee must pay to acquire the stock.

The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of FASB

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Statement No. 123, Accounting for Stock-Based Compensation, to stock-based employee compensation.

	Six Months Ended June 30,	
	2004	2003
Net income(loss) as reported	\$ 286,475	\$ 38,140
Deduct: Total stock-based employee compensation Expense determined under fair value based method For all awards, net of related tax effects	--	(2,025)
Pro forma net loss	\$ 286,475	\$ 21,443
Earnings per share:		
Basic - as reported	\$.06	\$.01
Basic - pro forma	\$.06	\$.01
Diluted - as reported	\$.06	\$.01
Diluted pro forma	\$.06	\$.01

The fair value of these options was estimated at the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions used for grants after 1998, expected volatility of 70% to 96%, risk-free rate of 3.9% to 6.6%, no dividend yield and expected life of 5 to 8 years.

Item 2.

MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Results of Operations

Quarter ended June 30, 2004 vs 2003:

Sales for the second quarter of 2004 increased by \$ 499,178 or 8.8% when compared to the corresponding quarter of 2003. This was the result of a \$ 531,101 increase in jewelry sales and a \$ 31,923 decrease in precious metals sales. These changes were due to a nation-wide improvement in the retail environment and price decreases in precious metal products. Pawn service fees increased by 13.1% due to an increase in loan volume. Cost of sales increased primarily due to the increase in sales. Gross margins increased from 19.0% in 2003 to 19.2% in 2004 due to the increase in sales of jewelry products.

Income taxes are provided at the corporate rate of 34% for both 2004 and 2003

Loss from discontinued operations during 2004 and 2003 in the amount of \$ 46,106 and \$ 24,444 net of income taxes is the combined results of three subsidiaries of the Company, DLS Financial Services, Inc., eye media, inc. and Silverman Consultants, Inc. The operations of these companies have been discontinued.

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Six months ended June 30, 2004 vs 2003:

Sales for the six months ended June 30, 2004 increased by \$ 2,150,585 or 20.0% when compared to the corresponding period of 2003. This was the result of a \$ 1,552,294 increase in jewelry sales and a \$ 598,291 increase in precious metals sales. These changes were due to a nation-wide improvement in the retail environment and price increases in precious metal products during the first quarter of 2004. Pawn service fees increased by 13.4% due to an increase in loan volume. Cost of sales increased primarily due to the increase in sales. Gross margins increased from 18.8% in 2003 to 19.2% in 2004 due to the increase in sales of jewelry products.

Income taxes are provided at the corporate rate of 34% for both 2004 and 2003

Loss from discontinued operations during 2004 and 2003 in the amount of \$ 78,101 and \$ 58,803 net of income taxes is the combined results of three subsidiaries of the Company, DLS Financial Services, Inc., eye media, inc. and Silverman Consultants, Inc. The operations of these companies have been discontinued.

Liquidity and Capital Resources

The Company's short-term debt totaled \$2,741,758 as of June 30, 2004. The ability of the Company to finance its operations and working capital needs are dependent upon management's ability to negotiate extended terms or refinance its short-term debt. The Company has historically renewed, extended or replaced short-term debt as it matures and management believes that it will be able to do so in the future as short-term debt matures.

Management of the Company expects capital expenditures to total approximately \$50,000 during the balance of 2004. It is anticipated that these expenditures will be funded from working capital.

From time to time, management has adjusted the Company's inventory levels to meet seasonal demand or in order to meet working capital requirements. Management is of the opinion that if additional working capital is required, additional loans can be obtained from individuals or from commercial banks. If necessary, inventory levels may be adjusted or a portion of the Company's investments in marketable securities may be liquidated in order to meet working capital requirements.

Contractual Cash Obligations

	Total	Payments due by year end			
	-----	2004	2005	2006	2007
	-----	-----	-----	-----	-----
Notes payable	\$2,741,758	\$ 266,758	\$2,475,000	--	--
Long-term debt and capital leases	1,419,651	198,122	\$ 484,737	\$ 137,906	\$ 135,33
Federal income taxes	360,568	360,568	--	--	--
Operating leases	295,504	117,047	148,205	18,886	11,36
	-----	-----	-----	-----	-----
	\$4,817,481	\$ 947,507	\$2,757,942	\$ 156,792	\$ 146,69
	=====	=====	=====	=====	=====

This report contains forward-looking statements which reflect the view of Company's management with respect to future events. Although management believes

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that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct. Important factors that could cause actual results to differ materially from such expectations are a down turn in the current strong retail climate and the potential for fluctuations in precious metals prices. The forward-looking statements contained herein reflect the current views of the Company's management and the Company assumes no obligation to update the forward-looking statements or to update the reasons actual results could differ from those contemplated by such forward-looking statements.

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ITEM 3. Controls and Procedures

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures within 90 days of the filing date of this quarterly report, and, based on their evaluation, our principal executive officer and principal financial officer have concluded that these controls and procedures are effective. There are no significant changes in our internal controls or other factors that could significantly affect these controls subsequent to the date of their evaluation. Disclosure controls and procedures are our controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time period specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file under the Exchange Act is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

PART II. OTHER INFORMATION

Item 4. Submission of Matters to a Vote of Security Holders.

The annual meeting of shareholders of the Company was held on June 21, 2004. Shareholders were asked to vote upon the election of directors and the approval of the Company's Stock option plan. The following is a tabulation of votes cast at the meeting:

	For -----	Against -----	Abstain -----
Election of Directors			
L.S. Smith	4,675,119	2,299	
W.H. Oyster	4,599,698	2,299	
John Benson	4,599,698	537	
James Walsh	4,599,698	537	
William Cordeiro	4,599,698	537	
Approval of Stock Option Plan	4,641,198	40,650	532

As a result of the vote, all persons named above were elected as directors and the Company's Stock option plan was approved.

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Item 6. Exhibits and Reports on Form 8-K.

Exhibits:

31.1 Certificate of L.S. Smith pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, Chief Executive Officer.

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31.2 Certificate of John Benson pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, Chief Financial Officer .

32.2 Certificate of L.S. Smith pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, Chief Executive Officer.

32.2 Certificate of John Benson pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, Chief Financial Officer.

Reports on Form 8-K :

8-K dated July 30, 2004
Item reported:

Acquisition or Disposition of Assets:

On July 28, 2004 DGSE COMPANIES, INC. ("the Company") sold the goodwill, trade name and other non-financial assets of the Company's wholly owned subsidiary Silverman Consultants, Inc. involved in the business of conducting in-store liquidation for others. These assets were purchased by Silverman Group, LLC ("the Buyer"). The Buyer is unrelated to the Company or to any officer or director of the Company. The Company's cost basis in the assets sold was \$314,000. The purchase price for these assets is based on a percentage of Silverman's revenues over the next five years to a maximum of \$ 600,000 and a minimum of \$ 400,000 with \$ 150,000 paid at closing and a note for the remaining balance.

SIGNATURES

In accordance with Section 13 and 15(d) of the Exchange Act, the Registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

DGSE Companies, Inc.

By: /s/ L. S. Smith Dated: August 6, 2004

L. S. Smith
Chairman of the Board,
Chief Executive Officer and
Secretary

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the date indicated.

By: /s/ L. S. Smith Dated: August 6, 2004

L. S. Smith
Chairman of the Board,
Chief Executive Officer and
Secretary

By: /s/ W. H. Oyster Dated: August 6, 2004

W. H. Oyster
Director, President and
Chief Operating Officer

By: /s/ John Benson Dated: August 6, 2004

John Benson
Chief Financial Officer
(Principal Accounting Officer)

