FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON D.C. 20549

(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, 1998

OR

( ) TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _______________ to _______________

For Quarter Ended June 30, 1998 Commission File number 2-71058

DAWSON GEOPHYSICAL COMPANY
(Exact name of Registrant as specified in its Charter)

| | |
|---|---|
| TEXAS | 75-0970548 |
| (State or other jurisdiction of incorporation or organization) | (IRS Employer Identification No.) |
| 508 West Wall, Suite 800, Midland, Texas | 79701 |
| (Address of principal executive offices) | (Zip Code) |

(Registrant's telephone number, including area code) 915/684-3000

NONE
(Former Name, Former Address & Former Fiscal Year if changed since last report)

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 June 30, 1998 |
|---|---|
| Common Stock, $.33 1/3 par value | 5,356,000 shares |

DAWSON GEOPHYSICAL COMPANY

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# PART I. FINANCIAL INFORMATION

## DAWSON GEOPHYSICAL COMPANY

## STATEMENTS OF OPERATIONS
(UNAUDITED)

| | Three Months Ended June 30 | | Nine Months Ended June 30 | |
|---|---|---|---|---|
| | 1998 | 1997 | 1998 | 1997 |
| Operating revenues | $ 18,647,000 | $ 12,520,000 | $ 45,991,000 | $ 34,304,000 |
| Operating costs: | | | | |
| Operating expenses | 11,193,000 | 8,127,000 | 30,094,000 | 22,840,000 |
| General and administrative | 478,000 | 386,000 | 1,443,000 | 1,052,000 |
| Depreciation | 2,461,000 | 1,685,000 | 6,816,000 | 5,456,000 |
| | 14,132,000 | 10,198,000 | 38,353,000 | 29,348,000 |
| Income from operations | 4,515,000 | 2,322,000 | 7,638,000 | 4,956,000 |
| Other income (expense): | | | | |
| Interest income | 209,000 | 86,000 | 579,000 | 167,000 |
| Interest expense | -- | (111,000) | (125,000) | (341,000) |
| Gain on disposal of assets | 19,000 | 3,000 | 167,000 | 196,000 |
| Other income | 5,000 | 6,000 | 28,000 | 15,000 |
| Income before income tax | 4,748,000 | 2,306,000 | 8,287,000 | 4,993,000 |
| Income tax expense: | | | | |
| Current | (1,386,000) | (622,000) | (2,333,000) | (1,222,000) |
| Deferred | (275,000) | (183,000) | (567,000) | (523,000) |
| | (1,661,000) | (805,000) | (2,900,000) | (1,745,000) |
| Net income | $ 3,087,000 | $ 1,501,000 | $ 5,387,000 | $ 3,248,000 |
| Net income per common share | $ .58 | $ .36 | $ 1.05 | $ .78 |
| Net income per common share--assuming dilution | $ .57 | $ .36 | $ 1.04 | $ .77 |
| Weighted average equivalent shares outstanding | 5,353,582 | 4,199,247 | 5,136,652 | 4,177,432 |
| Weighted average equivalent shares outstanding--assuming dilution | 5,379,341 | 4,214,035 | 5,165,082 | 4,201,552 |

See accompanying notes to the financial statements.

# DAWSON GEOPHYSICAL COMPANY

## BALANCE SHEETS

| | June 30, 1998 | September 30, 1997 |
|---|---|---|
| | (UNAUDITED) | |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 2,473,000 | $ 4,774,000 |
| Marketable securities | 6,527,000 | 3,968,000 |
| Accounts receivable | 13,104,000 | 8,724,000 |
| Prepaid expenses | 549,000 | 288,000 |
| Total current assets | 22,653,000 | 17,754,000 |
| Property, plant and equipment | 80,036,000 | 63,267,000 |
| Less accumulated depreciation | (33,996,000) | (27,460,000) |
| Net property, plant and equipment | 46,040,000 | 35,807,000 |
| | $ 68,693,000 | $ 53,561,000 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Current maturities of long-term debt | $ -- | $ 1,690,000 |
| Accounts payable | 1,542,000 | 3,956,000 |
| Accrued liabilities: | | |
| Payroll and other taxes | 380,000 | 566,000 |
| Other | 497,000 | 494,000 |
| Total current liabilities | 2,419,000 | 6,706,000 |
| Long-term debt, less current maturities | -- | 7,893,000 |
| Deferred income taxes | 1,984,000 | 1,417,000 |
| Stockholders' equity: | | |
| Preferred stock - par value $1.00 per share; 5,000,000 shares authorized, none outstanding | -- | -- |
| Common stock - par value $.33 1/3 per share; 10,000,000 shares authorized, 5,356,000 and 4,199,250 shares issued and outstanding | 1,785,000 | 1,400,000 |
| Additional paid-in capital | 38,215,000 | 17,174,000 |
| Retained earnings | 24,290,000 | 18,971,000 |
| Total stockholders' equity | 64,290,000 | 37,545,000 |
| | $ 68,693,000 | $ 53,561,000 |

Contingencies (See Note 3)

See accompanying notes to the financial statements.

DAWSON GEOPHYSICAL COMPANY

STATEMENTS OF CASH FLOWS

(UNAUDITED)

| | Nine Months Ended June 30 | |
|---|---|---|
| | 1998 | 1997 |
| Cash flows from operating activities: | | |
| Net income | $ 5,387,000 | $ 3,248,000 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 6,816,000 | 5,456,000 |
| Gain on disposal of assets | (167,000) | (196,000) |
| Other | 99,000 | (3,000) |
| Deferred income tax expense | 567,000 | 523,000 |
| Change in current assets and liabilities: | | |
| Increase in accounts receivable | (4,380,000) | (2,293,000) |
| Increase in prepaid expenses | (261,000) | (145,000) |
| Decrease in income taxes receivable | -- | 193,000 |
| Decrease in accounts payable | (2,414,000) | (519,000) |
| Decrease in accrued liabilities | (183,000) | (113,000) |
| Increase in federal and state income taxes payable | -- | 174,000 |
| Net cash provided by operating activities | 5,464,000 | 6,325,000 |
| Cash flows from investing activities: | | |
| Proceeds from disposal of assets | 264,000 | 288,000 |
| Capital expenditures | (17,322,000) | (2,340,000) |
| Proceeds from sale and maturity of marketable securities | 14,993,000 | 742,000 |
| Investment in marketable securities | (17,531,000) | (3,377,000) |
| Net cash used in investing activities | (19,596,000) | (4,687,000) |
| Cash flows from financing activities: | | |
| Principal payments on debt | (9,583,000) | (643,000) |
| Issuance of common stock | 21,371,000 | -- |
| Proceeds from exercise of stock options | 43,000 | 157,000 |
| Net cash provided (used) by financing activities | 11,831,000 | (486,000) |
| Net increase (decrease) in cash and cash equivalents | (2,301,000) | 1,152,000 |
| Cash and cash equivalents at beginning of period | 4,774,000 | 1,493,000 |
| Cash and cash equivalents at end of period | $ 2,473,000 | $ 2,645,000 |

See accompanying notes to the financial statements.

DAWSON GEOPHYSICAL COMPANY

NOTES TO FINANCIAL STATEMENTS

1. OPINION OF MANAGEMENT

Although the information furnished is unaudited, in the opinion of management of the Registrant, the accompanying financial statements reflect all adjustments (consisting only of normal recurring accruals) necessary for a fair presentation of the financial condition and results of operations for the periods presented. The results of operations for the three months and the nine months ended June 30, 1998, are not necessarily indicative of the results to be expected for the fiscal year.

2. NOTES PAYABLE

In April 1997, the Company entered into a loan agreement, as amended (the "Loan Agreement"), with a bank. The Loan Agreement consists of (1) a revolving line of credit of $6,000,000 which matures on April 15, 1999, (2) a term note in the aggregate principal amount of $6,000,000 bearing interest at the bank's prime rate and which matures on March 25, 2003 and (3) a term note in the aggregate principal amount of $5,000,000 bearing interest at the prime rate as published in The Wall Street Journal and which matures on April 15, 2003. The notes are secured by eligible accounts receivable and equipment purchased from loan proceeds.

On November 25, 1997, the Company repaid all outstanding principal and interest on the two Term Promissory Notes which have no reborrowing capacity. The Company has not utilized the revolving line of credit.

3. CONTINGENCIES

The Company is a defendant in two lawsuits pending in the 112th and 83rd District Courts of Pecos County, Texas relating to a July 1995 accident involving a van owned by the Company which was used to transport employees to various job sites and a non-Company owned vehicle. The accident resulted in the deaths of four Company employees who were passengers in such van. The Company is one of several named defendants in such suits. Other named defendants include the estate of the deceased driver of such van, who was an employee of the Company, the driver of such non-Company owned vehicle, who was then an employee of the Company, the owner of such vehicle, and Ford Motor Company, the manufacturer of the Company van involved in such accident. In general, the claims against the Company include allegations of negligence, gross negligence and/or intentional tort as a result of, among other things, the Company's alleged failure to provide safe transportation for its employees and to properly select, train and supervise the deceased driver of such van. The plaintiffs in such suits are seeking actual damages from the defendants of $15.5 million, additional unspecified actual damages, prejudgment and post-judgment interest and costs of suit as well as exemplary and punitive damages in an amount not to exceed four times the amount of actual damages. The Company believes that it has meritorious defenses to the

Notes to Financial Statements (continued)

claims asserted against it in such suits and it intends to continue to vigorously defend itself against such claims. In addition, the Company believes that it has approximately $11 million of liability insurance coverage to provide against an unfavorable outcome. Due to the uncertainties inherent in litigation, no assurance can be given as to the ultimate outcome of such suits or the adequacy or availability of the Company's liability insurance to cover the damages, if any, which may be assessed against the Company is such suits. A judgment awarding plaintiffs an amount significantly exceeding the Company's available insurance coverage could have a material adverse effect on the Company's financial condition, results of operations and liquidity.

The Company is party to other legal actions arising in the ordinary course of its business, none of which management believes will result in a material adverse effect on the Company's financial position or results of operation, as the Company believes it is adequately insured.

4. PUBLIC OFFERING

On November 21, 1997, the Company completed an offering of 1,150,000 shares. The proceeds of the offering were approximately $21,371,000 after deducting costs payable by the Company.

5. NET INCOME PER COMMON SHARE

| | Three Months Ended June 30 | | Nine Months Ended June 30 | |
|---|---|---|---|---|
| | 1998 | 1997 | 1998 | 1997 |
| Numerator: | | | | |
| Net income and numerator for basic and diluted net income per common share-income available to common stockholders | $3,087,000 | $1,501,000 | $5,387,000 | $3,248,000 |
| Denominator: | | | | |
| Denominator for basic net income per common share-weighted average common shares | 5,353,582 | 4,199,247 | 5,136,652 | 4,177,432 |
| Effect of dilutive securities-employee stock options | 25,759 | 14,788 | 28,430 | 24,120 |
| Denominator for diluted net income per common share-adjusted weighted average common shares and assumed conversions | 5,379,341 | 4,214,035 | 5,165,082 | 4,201,552 |
| Basic net income per common share | $ .58 | $ .36 | $ 1.05 | $ .78 |
| Diluted net income per common share | $ .57 | $ .36 | $ 1.04 | $ .77 |

# MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

## OVERVIEW

The results of operations for the three months ended June 30, 1998 are indicative of near-perfect operating conditions along with continued strong demand for the Company's 3-D seismic services. Hot and dry weather, favorable permitting and relatively large prospects contributed to minimal down time and optimal operating results. As the Company continues to enjoy favorable weather during the fourth quarter of fiscal 1998, it is experiencing typical transitions as crews complete one prospect and move to another. In May 1998, a 3,100-channel Input/Output System Two Remote Recording System (RSR) became productive, replacing the Halliburton MDS-18X recording system. With this upgrade the Company operates four Input/Output System Two conventional cable connected telemetry systems and two RSR systems. Capital expenditures for fiscal 1998 of $17,322,000 are comprised of the system upgrade, additional data channels for the existing crews, automotive units, and peripheral equipment. In November 1997, the Company completed a secondary public offering of 1,150,000 common shares with net proceeds of $21,371,000. In reviewing the Company's financial statements it should be noted that quarterly fluctuations in the Company's results of operations can occur due to weather, land use permitting and other factors.

## RESULTS OF OPERATIONS

The Company's operating revenues for the first nine months of 1998 totaled $45,991,000 versus $34,304,000 for the same period of fiscal 1997, an increase of 34.1%. For the three months ended June 30, 1998, operating revenues totaled $18,647,000 versus $12,520,000 for the same period of fiscal 1997, an increase of 48.9%. The increase for the nine-month period reflects the Company's added production capacity in response to continued strong demand for 3-D seismic services. In August 1997, the Company added its first RSR system to bring the number of crews to six. To further complement capacity, the Company has continually added channels to each of its crews. The increase in the quarter ended June 30, 1998 versus the same period of fiscal 1997 reflects the near-perfect conditions described above in the Overview.

Operating expenses for the nine months ended June 30, 1998 totaled $30,094,000, an increase of $7,254,000, or 31.8%, over the same period of fiscal 1997. For the quarter ended June 30, 1998, operating expenses increased $3,066,000, or 37.7%. Operating expenses increased primarily as a result of increased personnel and other expenses associated with equipment acquisitions and technological upgrades.

General and administrative expenses for the nine months ended June 30, 1998 totaled $1,443,000, an increase of $391,000 from the same period of fiscal 1997. For the quarter ended June 30, 1998, general and administrative expenses totaled $478,000, an increase of $92,000 from the same quarter of fiscal 1997. The increase primarily reflects additional personnel required to support expanding operations. Due to the Company's significant growth in recent years, the office building occupied since 1960 became outgrown, and the functions performed in that building have been moved to a facility that accommodates the Company's continued growth. General and administrative expenses totaled 3.1% of operating revenues for the nine months ended June 30, 1998 as well as for the same period of the prior year.

Depreciation for the nine months ended June 30, 1998 totaled $6,816,000, an increase of $1,360,000 from the same period of fiscal 1997. For the quarter ended June 30, 1998, depreciation increased $776,000, or 46.1%. Depreciation increased as a result of the capital expansion discussed below in "Liquidity and Capital Resources."

Total operating costs for the first nine months of fiscal 1998 totaled $38,353,000, an increase of 30.7%, from the same period of fiscal 1997 due to the factors described above. For the quarter ended June 30, 1998, operating costs increased 38.6% from the same period of the prior year. These increases are consistent with the high proportion of relatively fixed total operating costs (including personnel costs and depreciation) in conjunction with the addition of the Company's sixth crew in August 1997. Income from operations of $4,515,000 represents 24.2% of revenues for the three months ended June 30, 1998 as compared to a ratio of 18.5% for the same period of the prior year. For the nine-month periods of fiscal years 1998 and 1997, the ratios of income from operations to revenues are 16.6% and 14.4% respectively.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flows

Net cash provided by operating activities for the nine months ended June 30, 1998 of $5,464,000 as compared to $6,325,000 for the same period of the prior year is a decrease of $861,000. The net decrease is due to fluctuations in working capital components as net income and depreciation increased for the first nine months of fiscal 1998 as compared to the same period of fiscal 1997. The increase in accounts receivable reflects increased activity, and accounts receivable are considered collectible.

Net cash used in investing activities increased to $19,596,000 from $4,687,000 resulting from investment of offering proceeds and increased capital expenditures in the first nine months of fiscal 1998 as compared to the same period of fiscal 1997.

The cash flows provided by financing activities for the fiscal 1998 represent the net of the offering proceeds reduced by the retirement of debt.

Capital Expenditures

The Company continually strives to supply market demand with technologically advanced 3-D data acquisition recording systems and leading edge data processing capabilities. In April of 1998 the Company announced the purchase of a 3,100-channel

Input/Output System Two Remote Recording System to replace the Halliburton MDS-18X recording system. The approximate cost of the new system is $5,000,000. Capital expenditures to date of $17,322,000 include the new system as well as additions and replacements of cables and geophones, vehicles and other peripheral equipment. For the remainder of fiscal 1998, the Company anticipates the purchase of seismic data processing hardware and software, ancillary seismic data acquisition instrumentation, and leasehold improvements for the move of its corporate office. Depreciation has increased as a new crew has been placed into service each year for the past several years.

Capital Resources

The Company believes that its capital resources including its holdings of marketable securities, the availability of bank borrowings, and cash flow from operations are adequate to meet its current operational needs and finance capital needs as determined by market demand and technological developments.

Year 2000

The Company utilizes software and technologies throughout its operations that may be affected by the date change in the year 2000 (Year 2000 Issue). An assessment of the systems that will be affected by the Year 2000 Issue is underway. The Company does not believe the costs related the Year 2000 Issue will materially impact its results of operations. However, there can be no guarantee that the systems of other companies, on which the Company's systems rely, will be timely converted or that a failure to convert by another company or a conversion that is incompatible with the Company's systems would not have a material adverse effect on the Company.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

DAWSON GEOPHYSICAL COMPANY
(REGISTRANT)

By: /s/ L. Decker Dawson
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L. Decker Dawson
President

/s/ Christina W. Hagan
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Christina W. Hagan
Vice President and Chief Financial Officer

DATE: August 10, 1998
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# INDEX TO EXHIBITS


| EXHIBIT NUMBER | DESCRIPTION |
|---|---|
| 27 | Financial Data Schedule |
| 27.1 | Restated Financial Data Schedule |

5

9-MOS
SEP-30-1998
JUN-30-1998
2,473,000
6,527,000
13,104,000
0
0
22,653,000
80,036,000
(33,996,000)
68,693,000
2,419,000
0
0
0
1,785,000
0
68,693,000
45,991,000
45,991,000
38,353,000
38,353,000
0
0
(125,000)
8,287,000
(2,900,000)
5,387,000
0
0
0
5,387,000
1.05
1.04

5

| | |
|---|---|
| 9-MOS | 6-MOS |
| SEP-30-1997 | SEP-30-1997 |
| JUN-30-1997 | MAR-31-1997 |
| 2,645,000 | 1,249,000 |
| 3,680,000 | 3,632,000 |
| 8,454,000 | 7,240,000 |
| 0 | 0 |
| 0 | 0 |
| 15,072,000 | 12,398,000 |
| 55,225,000 | 54,396,000 |
| (25,550,000) | (23,697,000) |
| 44,747,000 | 43,097,000 |
| 3,182,000 | 3,001,000 |
| 0 | 0 |
| 0 | 0 |
| 0 | 0 |
| 1,400,000 | 1,400,000 |
| 0 | 0 |
| 36,220,000 | 34,719,000 |
| 34,304,000 | 21,784,000 |
| 34,304,000 | 21,784,000 |
| 29,348,000 | 19,150,000 |
| 29,348,000 | 19,150,000 |
| 0 | 0 |
| 0 | 0 |
| (341,000) | (230,000) |
| 4,993,000 | 2,687,000 |
| (1,745,000) | (940,000) |
| 3,248,000 | 1,747,000 |
| 0 | 0 |
| 0 | 0 |
| 0 | 0 |
| 3,248,000 | 1,747,000 |
| .78 | .42 |
| .77 | .42 |