

DGSE COMPANIES INC
Form 10-K
March 31, 2008

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-K

**FOR ANNUAL AND TRANSITION REPORTS PURSUANT TO SECTIONS 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934**

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

For the fiscal year ended December 31, 2007

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

Commission File No. 001-11048

DGSE COMPANIES, INC.

(Exact name of registrant as specified in its charter)

Nevada
(State or other jurisdiction of
incorporation or organization)

88-0097334
(I.R.S. Employer
Identification No.)

**11311 Reeder Road
Dallas, Texas 75229
972-484-3662**
(Address, including zip code, and telephone
number, including area code, of registrant's
principal executive offices)

Securities registered pursuant to Section 12(b) of the Act: **None**

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, par value \$.01 per share
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

YES NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.

YES NO

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 NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES NO

| | |
|--|----------------------|
| Aggregate market value of the 3,754,794 shares of Common Stock held by non-affiliates of the registrant at the closing sales price as reported on the National Association of Securities Dealers Automated Quotation System - National Market System on June 29, 2007 | \$ 13,667,450 |
|--|----------------------|

| | |
|--|------------------|
| Number of shares of Common Stock outstanding as of the close of business on March 27, 2008: | 9,938,037 |
|--|------------------|

Documents incorporated by reference:

Portions of the definitive proxy statement relating to the 2008 Annual Meeting of Stockholders of DGSE Companies, Inc. are incorporated by reference into Part III of this report.

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PART I

ITEM 1. BUSINESS.

Overview

Unless the context indicates otherwise, references to "we," "us" and "our" refers to the consolidated business operations of DGSE Companies, Inc., the parent, and all of its direct and indirect subsidiaries.

We buy and sell jewelry, bullion products and rare coins. Our customers include individual consumer, dealers and institutions throughout the United States. In addition, we make collateralized loans to individuals in the State of Texas. Our products and services are marketed through our facilities in Dallas and Euless, Texas; Mt. Pleasant, South Carolina; Beverly Hills, California and through our internet web sites DGSE.com; CGDEinc.com; SGBH.com; SuperiorPreciousMetals.com; SuperiorEstateBuyers.com; USBullionExchange.com; Americangoldandsilverexchange.com; and FairchildWatches.com.

We operate eight primary internet sites and over 900 related landing sites on the World Wide Web. Through the various sites we operate a virtual store, real-time auction of rare coin and jewelry products, free quotations of current prices on all commonly traded precious metal and related products, trading in precious metals, a mechanism for selling unwanted jewelry, rare coins and precious metals and wholesale prices and information exclusively for dealers on pre-owned fine watches. Over 7,500 items are available for sale on our internet sites including \$2,000,000 in diamonds.

Our wholly-owned subsidiary, National Pawn (f/k/a National Jewelry Exchange, Inc.), operates two pawn shops in Dallas, Texas. We have focused the subsidiary's operations on sales and pawn loans of jewelry products.

On May 9, 2007 we purchased all of the tangible assets of Euless Gold and Silver, Inc., located in Euless, Texas. We opened a new retail store in the former Euless Gold & Silver facility and operate under the name of Dallas Gold & Silver Exchange.

On May 30, 2007, we completed the acquisition of Superior Galleries, Inc. located in Beverly Hills, California. Superior's principal line of business is the sale of rare coins on a retail, wholesale, and auction basis. Superior's retail and wholesale operations are conducted in virtually every state in the United States. Superior also conducts live and interned auctions for customers seeking to sell their own coins. Superior markets its services nationwide through broadcast and print media and independent sales agents, as well as on the internet through third party websites, and through its own website at SGBH.com.

On July 13, 2007, we sold the loan balances from our American Pay Day Center locations and discontinued operations in those locations.

On August 3, 2007 we announced the launch of Americangoldandsilverexchange.com along with the simultaneous activation of over 900 proprietary Internet sites related to the home page of Americangoldandsilverexchange.com. This site, along with our existing locations in Texas, California and South Carolina, will provide customers from all over the United States with a safe and seamless way to value and sell gold, silver, rare coins, jewelry, diamonds and watches. We anticipate that Americangoldandsilverexchange.com will contribute to our growth and profitability in future periods.

Late in 2007, Superior Estate Buyers was launched to bring our unique expertise in the purchase of gold, silver, diamonds, rare coins and other collectibles to local markets with a team of traveling professionals for short-term buying events. It is our expectation that, over time, this activity will be expanded significantly with the objective of

having teams conducting events on a continuous basis.

Superior Precious Metals was also launched in late 2007 and it is the retail precious metals arm of DGSE. Professional account managers provide a convenient way for individuals and companies to buy and sell precious metals and rare coins. This activity is supported by the internally developed account management and trading platform created as part of DGSE's USBullionExchange.com precious metals system.

1

Products and Services

Our jewelry operations include sales to both wholesale and retail customers. We sell finished jewelry, gem stones, and findings (gold jewelry components) and make custom jewelry to order. Jewelry inventory is readily available from wholesalers throughout the United States. In addition, we purchase inventory from pawn shops and individuals. Jewelry repair is also available to our customers in our Dallas and Euless, Texas, Beverly Hills, California and Mt. Pleasant, South Carolina locations.

Our bullion and rare coin trading operations buy and sell all forms of precious metal products including United States and other government coins, medallions, art bars and trade unit bars. Bullion and rare coin transactions are conducted at all of our store locations.

Bullion and rare coin products are purchased and sold based on current market price. The availability of precious metal products is a function of price as virtually all bullion items are actively traded. Precious metals sales amounted to 33.6% of total revenues for 2007, 36.9% in 2006 and 30.0% in 2005.

During December 2000 we opened a new jewelry super store located in Mt. Pleasant, South Carolina. The store operates through a wholly owned subsidiary, Charleston Gold and Diamond Exchange, Inc. ("CGDE"). CGDE operates in a leased facility located in Mt. Pleasant, South Carolina.

We make pawn loans through our National Pawn locations. Pawn loans ("loans") are made on the pledge of tangible personal property, primarily jewelry, for one month with an automatic sixty-day extension period ("loan term"). Pawn service charges are recorded on a constant yield basis over the loan term. If the loan is not repaid, the principal amount loaned plus accrued pawn service charges become the carrying value of the forfeited collateral and are transferred to inventory.

Our primary presence on the internet is through our website DGSE.com. This web site serves as a corporate information site, a retail store where we sell our products and an auction site for jewelry and other products. The internet store functions as a CyberCash™ authorized site which allows customers to purchase products automatically and securely on line. Auctions close at least five times per week.

Our internet activity also includes a web site, USBullionExchange.com, which allows customers unlimited access to current quotations for prices on approximately 200 precious metals, coins and other bullion related products. This web site allows customers to enter immediate real-time buy and sell orders in dozens of precious metal products. This functionality allows our customers to fix prices in real time and to manage their precious metals portfolios in a comprehensive way.

We also offer wholesale customers a virtual catalog of our fine watch inventory through our web site Fairchildwatches.com.

We did not have any customer or supplier that accounted for more than 10% of total sales or purchases during 2007, 2006 or 2005.

Sales and Marketing

All of our activities rely heavily on local television, radio and print media advertising. Marketing activities emphasize our broad and unusual array of products and services and the attractiveness of its pricing and service.

We market our bullion and rare coin trading services through a combination of advertising in national coin publications, local print media, coin and bullion wire services and our internet web site. Trades are primarily with coin and bullion dealers on a "cash on confirmation" basis which is prevalent in the industry. Cash on confirmation means that once credit is approved the buyer remits funds by mail or wire concurrently with the mailing of the precious metals. Customer orders for bullion or rare coin trades are customarily delivered within three days of the order or upon clearance of funds depending on the customer's credit standing. Consequently, there was no significant backlog for bullion orders as of December 31, 2007, 2006 or 2005. Our backlogs for fabricated jewelry products were also not significant as of December 31, 2007, 2006 and 2005.

Seasonality

The retail and wholesale jewelry business is seasonal. We realized 37.2%, 27.7% and 41.8% of our annual sales in the fourth quarters of 2007, 2006 and 2005, respectively.

While our bullion and rare coin business is not seasonal, management believes it is directly impacted by the perception of inflation trends. Historically, anticipation of increases in the rate of inflation has resulted in higher levels of interest in precious metals as well as higher prices for such metals. Our other business activities are not seasonal.

Competition

We operate in a highly competitive industry where competition is based on a combination of price, service and product quality. Our jewelry and consumer loan activities compete with numerous other retail jewelers and consumer lenders in Dallas and Euless, Texas; Beverly Hills, California; and Mt. Pleasant, South Carolina and the surrounding areas.

The bullion and rare coin industry in which we compete is dominated by substantially larger enterprises which wholesale bullion, rare coin and other precious metal products.

We attempt to compete in all of our activities by offering high quality products and services at prices below that of our competitors and by maintaining a staff of highly qualified employees.

Employees

As of December 31, 2007, we employed 93 individuals, 91 of whom were full time employees.

Available Information

Our website is located at www.dgse.com. Through this website, we make available free of charge all of our Securities and Exchange Commission filings. In addition, a complete copy of our Code of Ethics is available through this website.

Discontinued Operations and Acquisitions

Discontinued Operations.

On July 13, 2007, we sold the loan balances from our American Pay Day Center locations for \$77,496 and discontinued operations in those locations. The receivables sold, including interest due, had a balance of \$120,573 at the time of the sale. The sales price was determined based on the age of the outstanding receivables. As a result of the sale and discontinued operations, we recognized a pretax loss of \$107,838 on the disposal and a pretax loss on discontinued operations of \$51,938 for the year ended December 31, 2007.

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Acquisitions.

Superior Galleries, Inc. On May 30, 2007, we completed our acquisition of Superior Galleries, Inc., which we refer to as Superior, pursuant to an amended and restated agreement and plan of merger and reorganization dated as of January 6, 2007, which we refer to as the merger agreement, with Superior and Stanford International Bank Ltd., then Superior's largest stockholder and its principal lender, which we refer to as Stanford, as stockholder agent for the Superior stockholders, whereby Superior became a wholly owned subsidiary of DGSE Companies, Inc. Superior operates a store in Beverly Hills, CA. The total purchase price of approximately \$13.6 million was broken down as follows:

| | Shares | Stock Price | Extended Price |
|---------------------------|-----------|---------------------|----------------|
| Common stock | 3,669,067 | \$ 2.55 | \$ 9,356,121 |
| A warrants | 845,634 | 1.27 ⁽¹⁾ | 1,073,955 |
| B warrants | 863,000 | 2.55 | 2,200,650 |
| Exercise Price B warrants | 863,000 | \$.001 | (863) |
| Direct transaction costs | | | 1,176,290 |
| Total purchase price | | | \$ 13,806,153 |

(1)The \$1.27 is the fair value of the warrants calculated under the Black Sholes method as of the acquisition date.

The total purchase price has been allocated to the fair value of assets acquired and liabilities assumed as follows:

| | |
|---------------------------|---------------|
| Goodwill | \$ 8,203,448 |
| Intangible assets | 2,521,340 |
| Deferred tax asset | 1,860,475 |
| Property and other assets | 1,068,958 |
| Inventory | 3,260,766 |
| Liabilities assumed | (3,108,834) |
| Total purchase price | \$ 13,806,153 |

In accordance with SFAS 142, the goodwill will not be amortized but instead tested for impairment in accordance with the provisions of SFAS 142 at least annually and more frequently upon the occurrence of certain events.

The operating results of Superior have been included in the consolidated financial statements since the acquisition date of May 30, 2007. The following unaudited pro forma condensed consolidated financial information reflects the results of operations for the year ended December 31, 2007 and 2006 as if the acquisition of Superior had occurred on January 1 of each year after giving effect to purchase accounting adjustments. These pro forma results have been prepared for comparative purposes only and do not purport to be indicative of what operating results would have been had the acquisition actually taken place at the beginning of the period, and may not be indicative of future operating results (in thousands, except per share data):

| <i>(In thousands, except per share data)</i> | Year Ended December 31, | |
|--|-------------------------|------------|
| | 2007 | 2006 |
| | (Unaudited) | |
| Pro forma total revenue | \$ 73,565 | \$ 83,487 |
| Pro forma net earnings (loss) | \$ (2,920) | \$ (3,135) |
| Pro forma net earnings per share — basic | \$ (.33) | \$ (0.50) |
| Pro forma net earnings per share — diluted | \$ (.33) | \$ (0.50) |
| Pro forma weighted average shares — basic | 8,582 | 6,226 |

Pro forma weighted average shares — diluted

10,353

6,320

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In relation to the acquisition, as of June 29, 2007, Stanford and Dr. L.S. Smith, our chairman and chief executive officer, collectively had the power to vote approximately 63% of our voting securities, and beneficially owned approximately 56.4% of our voting securities on a fully-diluted basis (after giving effect to the exercise of all options and warrants held by them which are exercisable within sixty days of December 31, 2007 but not giving effect to the exercise of any other options or warrants). Consequently, these two stockholders have sufficient voting power to control the outcome of virtually all corporate matters submitted to vote of our common stockholders. Those matters could include the election of directors, changes in the size and composition of our board of directors, mergers and other business combinations involving us, or the liquidation of our company. In addition, Stanford and Dr. Smith have entered into a corporate governance agreement with us, which entitles Stanford and Dr. Smith to each nominate two "independent" directors to our board and entitles Dr. Smith, our chairman and chief executive officer, and William H. Oyster, our president and chief operating officer, to be nominated to our board for so long as each remains an executive officer.

Through this control of company nominations to our board of directors and through their voting power, Stanford and Dr. Smith are able to exercise substantial control over certain decisions, including decisions regarding the qualification and appointment of officers, dividend policy, access to capital (including borrowing from third-party lenders and the issuance of additional equity securities), a merger or consolidation with another company, and our acquisition or disposition of assets. Also, the concentration of voting power in the hands of Stanford and Dr. Smith could have the effect of delaying or preventing a change in control of our company, even if the change in control would benefit our other stockholders. The significant concentration of stock ownership may adversely affect the trading price of our common stock due to investors' perception that conflicts of interest may exist or arise.

Eules Gold & Silver, Inc.

On May 9, 2007 we purchased all of the tangible assets of Eules Gold and Silver, Inc., located in Eules, Texas. The purchase price paid for these assets totaled \$1,000,000 including \$600,000 in cash and a two year note in the amount of \$400,000. We opened a new retail store in the former Eules Gold & Silver facility and operate under the name of Dallas Gold & Silver Exchange. Of the assets received, \$990,150 was inventory and the remainder was fixed assets.

We entered into these transactions seeing them as opportunistic acquisitions that would allow us to expand our operations and provide a platform for future growth.

ITEM 1A. RISK FACTORS.

You should carefully consider the risks described below before making an investment decision. We believe these are all the material risks currently facing our business. Our business, financial condition or results of operations could be materially adversely affected by these risks. The trading price of our common stock could decline due to any of these risks, and you may lose all or part of your investment. You should also refer to the other information included or incorporated by reference in this report, including our financial statements and related notes.

Changes in customer demand for our products and services could result in a significant decrease in revenues.

Although our customer base commonly uses our products and services, our failure to meet changing demands of our customers could result in a significant decrease in our revenues.

Changes in governmental rules and regulations applicable to the specialty financial services industry could have a negative impact on our lending activities.

Our lending is subject to extensive regulation, supervision and licensing requirements under various federal, state and local laws, ordinances and regulations. New laws and regulations could be enacted that could have a negative impact on our lending activities.

Fluctuations in our inventory turnover and sales.

We regularly experience fluctuations in our inventory balances, inventory turnover and sales margins, yields on loan portfolios and pawn redemption rates. Changes in any of these factors could materially and adversely affect our profitability and ability to achieve our planned results.

Changes in our liquidity and capital requirements could limit our ability to achieve our plans.

We require continued access to capital, and a significant reduction in cash flows from operations or the availability of credit could materially and adversely affect our ability to achieve our planned growth and operating results. Similarly, if actual costs to build new stores significantly exceeds planned costs, our ability to build new stores or to operate new stores profitably could be materially restricted. The DGSE credit agreement also limits the allowable amount of capital expenditures in any given fiscal year, which could limit our ability to build new stores.

Changes in competition from various sources could have a material adverse impact on our ability to achieve our plans.

We encounter significant competition in connection with our retail and lending operations from other pawnshops, cash advance companies and other forms of financial institutions and other retailers, many of which have significantly greater financial resources than us. Significant increases in these competitive influences could adversely affect our operations through a decrease in the number or quality of payday loans and pawn loans or our ability to liquidate forfeited collateral at acceptable margins.

In the coins and other collectibles business, we will compete with a number of comparably sized and smaller firms, as well as a number of larger firms throughout the United States. Our primary competitors are Heritage Auction Galleries, a large scale coin dealer and auctioneer, and American Numismatic Rarities, a comparably-sized coin auctioneer. Many of our competitors have the ability to attract customers as a result of their reputation and the quality collectibles they obtain through their industry connections. Additionally, other reputable companies that sell or auction rare coins and other collectibles may decide to enter our markets to compete with us. These companies have greater name recognition and have greater financial and marketing resources than we do. If these auction companies

are successful in entering the specialized market for premium collectibles in which we participate or if dealers and sellers participate less in our auctions, we may attract fewer buyers and our revenue could decrease.

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Our earnings could be negatively impacted by an unfavorable outcome of litigation, regulatory actions, or labor and employment matters.

From time to time, we are involved in litigation, regulatory actions and labor and employment matters arising from our normal operations. Currently we are a defendant in several actions. Although we believe the resolution of these actions will not have a material adverse effect on our financial condition, results of operation or liquidity, there can be no assurance as to the ultimate outcome of these or future actions.

A failure in our information systems could prevent us from effectively managing and controlling our business or serving our customers.

We rely on our information systems to manage and operate our stores and business. Each store is part of an information network that permits us to maintain adequate cash inventory, reconcile cash balances daily and report revenues and expenses timely. Any disruption in the availability of our information systems could adversely affect our operation, the ability to serve our customers and our results of operations.

A failure of our internal controls and disclosure controls and procedures, or our inability to comply with the requirements of section 404 of the Sarbanes-Oxley Act in a timely fashion could have a material adverse impact on us and our investors' confidence in our reported financial information.

Effective internal controls and disclosure controls and processes are necessary for us to provide reliable financial reports and to detect and prevent fraud. We are currently performing the system and process evaluation required to comply with the management certification and auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act. This evaluation may conclude that enhancements, modifications or changes to our controls are necessary. Completing this evaluation, performing testing and implementing any required remedial changes will require significant expenditures and management attention. We cannot be certain as to the timing of completion of our evaluation, testing and remediation actions or the impact of these on our operations. We cannot be certain that significant deficiencies or material weaknesses will not be identified, or that remediation efforts will be timely to allow us to comply with the requirements of Section 404 of the Sarbanes-Oxley Act. If we are unable to comply with the requirements of Section 404 of the Sarbanes-Oxley Act, investors could lose confidence in our reported financial information.

This Annual Report on Form 10-K does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit the Company to provide only management's report in this Annual Report on Form 10-K.

Changes in general economic conditions could negatively affect loan performance and demand for our products and services.

A sustained deterioration in the economic environment could adversely affect our operations by reducing consumer demand for the products we sell.

Interest rate fluctuations could increase our interest expense.

Although the U.S. Federal Reserve halted a sustained period of regular interest rate hikes in August 2006, interest rates could continue to rise which would, in turn, increase our cost of borrowing.

Our success depends on our ability to attract, retain and motivate management and other skilled employees.

Our future success and growth depend on the continued services of our key management and employees. The loss of the services of any of these individuals or any other key employee or contractor could materially affect our business. Our future success also depends on our ability to identify, attract and retain additional qualified personnel. Competition for employees in our industry is intense and we may not be successful in attracting or retaining them. There are a limited number of people with knowledge of, and experience in, our industry. We do not have employment agreements with many of our key employees. We do not maintain life insurance policies on many of our employees. Our loss of key personnel, especially without advance notice, or our inability to hire or retain qualified personnel, could have a material adverse effect on sales and our ability to maintain our technological edge. We cannot guarantee that we will continue to retain our key management and skilled personnel, or that we will be able to attract, assimilate and retain other highly qualified personnel in the future.

The voting power in our company is substantially controlled by a small number of stockholders, which may, among other things, delay or frustrate the removal of incumbent directors or a takeover attempt, even if such events may be beneficial to our stockholders.

As of June 29, 2007, Stanford International Bank Ltd., which we refer to as Stanford, and Dr. L.S. Smith, our chairman and chief executive officer, collectively had the power to vote approximately 63% of our voting securities, and beneficially owned approximately 56.4% of our voting securities on a fully-diluted basis (after giving effect to the exercise of all options and warrants held by them which are exercisable within sixty days of December 31, 2007 but not giving effect to the exercise of any other options or warrants). Consequently, these two stockholders may have sufficient voting power to control the outcome of virtually all corporate matters submitted to the vote of our common stockholders. Those matters could include the election of directors, changes in the size and composition of our board of directors, mergers and other business combinations involving us, or the liquidation of our company. In addition, Stanford and Dr. Smith have entered into a corporate governance agreement with us, which entitles Stanford and Dr. Smith to each nominate two “independent” directors to our board and entitles Dr. Smith, our chairman and chief executive officer, and William H. Oyster, our president and chief operating officer, to be nominated to our board for so long as he remains an executive officer.

Through this control of company nominations to our board of directors and through their voting power, Stanford and Dr. Smith are able to exercise substantial control over certain decisions, including decisions regarding the qualification and appointment of officers, dividend policy, access to capital (including borrowing from third-party lenders and the issuance of additional equity securities), a merger or consolidation with another company, and our acquisition or disposition of assets. Also, the concentration of voting power in the hands of Stanford and Dr. Smith could have the effect of delaying or preventing a change in control of our company, even if the change in control would benefit our other stockholders. The significant concentration of stock ownership may adversely affect the trading price of our common stock due to investors’ perception that conflicts of interest may exist or arise.

We could be subject to sales taxes, interest and penalties on interstate sales for which we have not collected taxes.

Superior has not collected California sales tax on mail-order sales to out-of-state customers, nor has it collected use tax on its interstate mail order sales. We believe that our sales to interstate customers are generally tax-exempt due to varying state exemptions relative to the definitions of being engaged in business in particular states and the lack of current Internet taxation. While we have not been contacted by any state authorities seeking to enforce sales or use tax regulations, we cannot assure you that we will not be contacted by authorities in the future with inquiries concerning our compliance with current statutes, nor can we assure you that future statutes will not be enacted that affect the sales and use tax aspects of our business.

We may incur losses as a result of accumulating inventory.

In addition to auctioning rare coins on consignment, a substantial portion of the rare coins that Superior sells comes from its own inventory. Superior purchases these rare coins from dealers and collectors and assumes the inventory and price risks of these items until they are sold. If Superior is unable to resell the rare coins that it purchases when it wants or needs to, or at prices sufficient to generate a profit from their resale, or if the market value of the inventory of purchased rare coins were to decline, our revenue would likely decline.

If we experience an increase in the rescission of sales, our revenue and profitability could decrease.

Our operating results could suffer if we experience a significant increase in the number of sales that are rescinded due to questions about title, provenance or authenticity of an item. Superior warrants the title, provenance and authenticity of each item that it sells at auction. A buyer who believes that any of these characteristics is in doubt must notify Superior in writing within a certain number of days after the date of sale of the property. If Superior cannot substantiate the questioned characteristics, the buyer may rescind the purchase and Superior will refund the price paid at auction to the buyer. When a purchase is rescinded, the seller is required to refund the item's sale price less sellers' commissions and other sellers' fees.

Our planned expansion and enhancement of our website and internet operations may not result in increased profitability.

The satisfactory performance, reliability and availability of our website and network infrastructure are and will be critical to our reputation and our ability to attract and retain customers and technical personnel and to maintain adequate customer service levels. Any system interruptions or reduced performance of our website could materially adversely affect our reputation and our ability to attract new customers and technical personnel. We are in the process of development and/or enhancement of several portions of our websites that will offer content and auctions for rare coins that may have a lower average selling price than many of the rare coins in the markets we currently serve, and in the future we plan to integrate various of our websites. Continued development of our websites will require significant resources and expense. If the planned expansion of our websites does not result in increased revenue, we may experience decreased profitability.

Our websites may be vulnerable to security breaches and similar threats which could result in our liability for damages and harm to our reputation.

Despite the implementation of network security measures, our websites are vulnerable to computer viruses, break-ins and similar disruptive problems caused by internet users. These occurrences could result in our liability for damages, and our reputation could suffer. The circumvention of our security measures may result in the misappropriation of customer or other confidential information. Any such security breach could lead to interruptions and delays and the cessation of service to our customers and could result in a decline in revenue and income.

Changes to financial accounting standards and new exchange rules could make it more expensive to issue stock options to employees, which would increase compensation costs and may cause us to change our business practices.

We prepare our financial statements to conform with generally accepted accounting principles, or GAAP, in the United States. These accounting principles are subject to interpretation by the Public Company Accounting Oversight Board, the SEC and various other bodies. A change in those policies could have a significant effect on our reported results and may affect our reporting of transactions completed before a change is announced.

We are subject to new corporate governance and internal control reporting requirements, and our costs related to compliance with, or our failure to comply with existing and future requirements could adversely affect our business.

We face new corporate governance requirements under the Sarbanes-Oxley Act of 2002, as well as new rules and regulations subsequently adopted by the SEC, the Public Company Accounting Oversight Board and the American Stock Exchange. These laws, rules and regulations continue to evolve and may become increasingly stringent in the future. In particular, we will be required to include management's report on internal controls as part of our annual report for the year ending December 31, 2007 pursuant to Section 404 of the Sarbanes-Oxley Act. We are in the

process of evaluating our control structure to help ensure that we will be able to comply with Section 404 of the Sarbanes-Oxley Act. We cannot assure you that we will be able to fully comply with these laws, rules and regulations that address corporate governance, internal control reporting and similar matters. Failure to comply with these laws, rules and regulations could materially adversely affect our reputation, financial condition and the value and liquidity of our securities.

The revolving credit facilities with Stanford International Bank Ltd. and Texas Capital Bank, N.A. is each collateralized by a general security interest in our assets. If we were to default under the terms of either credit facility, the lender would have the right to foreclose on our assets.

In December 2005, we entered into a revolving credit facility with Texas Capital Bank, N.A., which currently permits borrowings up to a maximum principal amount of \$4.3 million. Borrowings under the revolving credit facility are collateralized by a general security interest in substantially all of our assets (other than the assets of Superior). As of December 31, 2007, approximately \$4.2 million was outstanding under the term loan and revolving credit facility. If we were to default under the terms and conditions of the revolving credit facility, Texas Capital Bank would have the right to accelerate any indebtedness outstanding and foreclose on our assets in order to satisfy our indebtedness. Such a foreclosure could have a material adverse effect on our business, liquidity, results of operations and financial position.

In October 2003, Superior entered into a revolving credit facility with Stanford Financial Group Company, which we refer to as SFG, which has assigned the facility to Stanford. The facility currently permits borrowings up to a maximum principal amount of \$11.5 million, up to \$6 million of which Superior may upstream to DGSE. Borrowings under the revolving credit facility are collateralized by a general security interest in substantially all of Superior's assets and, to the extent of money upstreamed to DGSE, substantially all of DGSE's assets. As of December 31, 2007, approximately \$6.7 million was outstanding under the revolving credit facility. If Superior were to default under the terms and conditions of the revolving credit facility, Stanford would have the right to accelerate any indebtedness outstanding and foreclose on Superior's assets, and, subject to intercreditor arrangements with Texas Capital Bank and other limitations, our assets, in order to satisfy Superior's indebtedness. Such a foreclosure could have a material adverse effect on our business, liquidity, results of operations and financial position.

We have not paid dividends on our common stock in the past and do not anticipate paying dividends on our common stock in the foreseeable future.

We have not paid common stock dividends since our inception and do not anticipate paying dividends in the foreseeable future. Our current business plan provides for the reinvestment of earnings in an effort to complete development of our technologies and products, with the goal of increasing sales and long-term profitability and value. In addition, our revolving credit facility with Texas Capital Bank currently restricts, and any other credit or borrowing arrangements that we may enter into may in the future restrict or limit, our ability to pay dividends to our stockholders.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None.

ITEM 2. PROPERTIES.

We own a 20,000 square foot facility at 11311 Reeder Rd, Dallas, Texas which houses retail and wholesale jewelry, bullion and rare coin trading operations and our principal executive offices. The land and buildings are subject to a mortgage maturing in August 2016, with a balance outstanding of approximately \$2,435,364 as of December 31, 2007.

Our Euless, TX location is a 2,158 square foot facility which houses retail jewelry, bullion and rare coin trading operations. Our monthly lease payments at December 31, 2007 are 2,518 and the lease is due to expire June 30, 2010.

At December 31, 2007 we were leasing two facilities in Dallas, Texas which house our National Pawn operations. The two pawn locations are 4,700 square feet and 6,800 square feet, respectively. The leases are due to expire on December 31, 2009 and October 31, 2012 and require monthly lease payments in the amount of \$6,552 and 7,997, respectively.

CGDE operates in a leased 2,367 square foot facility in Mt. Pleasant, South Carolina. The lease expires in June 2010 and requires monthly lease payments in the amount of \$4,575.

Our Superior Galleries operations are located in an approximately 7,000 square foot storefront facility located at 9478 West Olympic Boulevard, Beverly Hills, California. This facility includes administrative, customer support, auction, gallery and retail space. One lease for the store front lease expires on September 30, 2012; and one lease for the office space expires July 31, 2010. The combined monthly rental rate is \$29,656 including parking fees and rent of storage space, subject to annual increases based on increases in the consumer price index.

We also maintain a resident agent office in Nevada at the office of our Nevada counsel, McDonald, Carano, Wilson, McClure, Bergin, Frankovitch and Hicks, 241 Ridge Street, Reno, Nevada 89505.

ITEM 3. LEGAL PROCEEDINGS.

On June 6, 2006 Superior Galleries was sued in the U.S. District Court for Central California by Elaine and Dean Sanders in connection with a loan made to them against 32 coins placed on consignment on June 26, 2004. Fourteen of the coins were sold, and the proceeds from this sale of approximately \$186,750 were insufficient to repay the remaining loan balance of \$359,471 that Superior made to the Sanders. The plaintiffs subsequently paid an additional \$155,000 in December 2005 with respect to the loan, but now allege that Superior violated its agreement with them relating to the sale of the coins. Superior strongly denies that it violated the agreement or that it acted improperly in any way. This litigation was settled in December 2007 with Superior agreeing to pay Elaine and Dean Sanders \$30,000 in cash.

In April 2004 Superior sued its former Chief Financial Officer, Malingham Shrinivas, in Los Angeles Superior Court for breach of contract, fraud and conspiracy. In that lawsuit, Superior alleged that he fraudulently arranged to receive more salary than he was entitled to, to pay personal expenses using Superior's funds, and to pay third party vendors with Superior's funds for services which were not rendered. In July 2004 Mr. Shrinivas filed a counterclaim in this litigation, claiming that he was terminated without just cause and was therefore entitled to \$58,250 in severance pay. Although the case had been scheduled for trial in August 2006, prior to that time the case was stayed by order of the Superior Court because the Court had been advised that criminal charges against Mr. Shrinivas related to this matter were imminent. Those criminal charges were subsequently filed and then dropped, and therefore further proceedings in connection with the civil case will continue, but a trial date has not been scheduled. Superior believes that Mr. Shrinivas was terminated with cause and that he is therefore not entitled to any severance pay. The stay of our civil case was lifted and mediation was held in November 2007 with no results. Superior intends to vigorously pursue its claims and defend Mr. Shrinivas' claims for severance pay.

On November 7, 2006 Superior was sued in the United States District Court for the Northern District of Texas by a competitor, Heritage Numismatic Auctions, Inc. (“Heritage”). In its complaint, Heritage alleges that Superior violated Heritage’s copyright rights by copying Heritage’s catalog descriptions of certain coins and currency offered for sale by Heritage. Heritage claims that these alleged actions also violate the California Unfair Competition Act. In December 2007 this litigation was settled with Superior agreeing to pay Heritage \$75,000 in cash and DGSE Companies, Inc. agreeing to issue 8,372 restricted common shares of its common stock, having a \$50,000 market value when issued in January 2008.

We may, from time to time, be involved in various claims, lawsuits, disputes with third parties, actions involving allegations of discrimination, or breach of contract actions incidental to the operation of its business. Except as set forth above, we are not currently involved in any such litigation which we believe could have a material adverse effect on our financial condition or results of operations, liquidity or cash flows.

PART II**ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.**

On October 31, 2007, our Common Stock began trading on the American Stock Exchange (“AMEX”) under the symbol “DGC”. Previously, our Common Stock was traded on the NASDAQ Small CAP Market under the symbol “DGSE”. The following table sets forth for the period indicated, the per share high and low bid quotations as reported by NASDAQ and AMEX for our common stock. During the past three years, we have not declared any dividends with respect to our common stock. We intend to retain all earnings to finance future growth; accordingly, it is not anticipated that cash dividends will be paid to holders of common stock in the foreseeable future.

The following quotations reflect inter-dealer prices without retail mark-ups, mark-downs or commissions and may not reflect actual transactions. High and low bid quotations for the last two years were:

| <u>2007</u> | | High | | Low |
|--------------------|----|-------------|----|------------|
| Fourth Quarter | \$ | 6.110 | \$ | 3.470 |
| Third Quarter | | 4.490 | | 3.050 |
| Second Quarter | | 4.100 | | 2.080 |
| First Quarter | | 3.000 | | 2.380 |
| <u>2006</u> | | High | | Low |
| Fourth Quarter | \$ | 4.480 | \$ | 2.100 |
| Third Quarter | | 3.340 | | 1.950 |
| Second Quarter | | 2.850 | | 2.090 |
| First Quarter | | 2.490 | | 1.500 |

On March 27, 2008, the closing sales price for our common stock was \$5.05 and there were 439 shareholders of record.

Securities authorized for issuance under equity compensation plans.

We have granted options to certain officers, directors and key employees to purchase shares of our common stock. Each option vests according to a schedule designed by our board of directors, not to exceed four years. Each option expires 180 days from the date of termination of the employee or director. The exercise price of each option is equal to the market value of our common stock on the date of grant. These option grants have been approved by security holders.

The following table summarizes options outstanding as of December 31, 2007:

| Plan Category | Number of securities to be issued upon exercise of options, warrants & rights | Weighted average exercise price of outstanding options, warrants & rights | Number of securities remaining available for future issuance under equity compensation plans |
|--|---|---|--|
| Equity compensation plans approved by security holders | 1,479,251 | \$ 2.34 | 700,000 |
| Equity compensation plans not approved by security holders | None | — | None |
| Total | 1,479,251 | \$ 2.34 | 700,000 |

Stock Performance Table

The following table represents a comparison of the five year total return of our common stock to the NASDAQ Composite Index, the S&P 600 Small Cap Index and the S&P Retail Index for the period from January 1, 2002 to December 31, 2007. The comparison assumes \$100 was invested on December 31, 2002 and dividends, if any, were reinvested for all years ending December 31.

Comparison of Five Year Cumulative Return

| Date: | DGSE Common Stock | NASDAQ Composite Index | S&P Retail Index | S&P 600 Small Cap Index |
|-------|----------------------|---------------------------|---------------------|----------------------------|
| 2002 | 100 | 100 | 100 | 100 |
| 2003 | 69 | 103 | 111 | 116 |
| 2004 | 83 | 111 | 136 | 142 |
| 2005 | 59 | 113 | 134 | 142 |
| 2006 | 75 | 124 | 146 | 172 |
| 2007 | 490 | 197 | 143 | 199 |

On June 27, 2006 stockholders of the Company approved the adoption of the 2006 Equity Incentive Plan (the "2006 Plan"). During the year ended December 31, 2007, there were 50,000 options granted to our non-employee directors under this plan and, as a result, there are 700,000 shares available for future grants under the 2006 Plan.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

CAUTIONARY STATEMENT REGARDING RISKS AND UNCERTAINTIES THAT MAY AFFECT FUTURE RESULTS

Forward-Looking Statements

This Annual Report on Form 10-K, including Management's Discussion and Analysis of Financial Condition and Results of Operations, includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements generally can be identified by the use of forward-looking terminology, such as "may," "will," "would," "expect," "intend," "could," "estimate," "should," "anticipate" or "believe." We intend that all forward-looking statements be subject to the safe harbors created by these laws. All statements other than statements of historical information provided herein are forward-looking and may contain information about financial results, economic conditions, trends, and known uncertainties. All forward-looking statements are based on current expectations regarding important risk factors. Many of these risks and uncertainties are beyond our ability to control, and, in many cases, we cannot predict all of the risks and uncertainties that could cause our actual results to differ materially from those expressed in the forward-looking statements. Actual results could differ materially from those expressed in the forward-looking statements, and readers should not regard those statements as a representation by us or any other person that the results expressed in the statements will be achieved. Important risk factors that could cause results or events to differ from current expectations are described under the section "Risk Factors" and elsewhere in this report. These factors are not intended to be an all-encompassing list of risks and uncertainties that may affect the operations, performance, development and results of our business. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. We undertake no obligation to release publicly the results of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date hereon, including without limitation, changes in our business strategy or planned capital expenditures, store growth plans, or to reflect the occurrence of unanticipated events.

Results of Operations

Comparison of the Years ended December 31, 2007 and 2006

Revenues increased by \$18,884,000, or 42.8%, in 2007. This increase was primarily the result of a \$4,901,000, or 30.1% increase in the sale of precious metals products, a \$2,819,000, or 17.1% increase in retail jewelry sales, a \$9,224,000, or 196.4% increase in rare coin sales, and auction revenues of \$1,498,000. The increases in precious metals, rare coin and jewelry sales were due to a 31.0% price increase in gold products and the acquisition of Superior Galleries and Eulless Gold and Silver. The auction revenues were the result of the acquisition of Superior Galleries. Consumer loan service fees increased by \$118,641 in 2007 due to increased loans outstanding during the year. Management fees in the amount of \$250,000 were derived from a management agreement between the Company and Superior Galleries prior to the acquisition. Cost of goods as a percentage of sales decreased to 82.9% in 2007 from 84.3% in 2006 and gross margins increased to 17.1% in 2007 from 15.7% in 2006. This increase was due to the higher margins on gold products and auction fees earned during 2007.

Selling, general and administrative expenses increased by \$4,196,134, or 75.9%. This increase was primarily due to the acquisition of Superior Galleries and Eulless Gold and Silver. These acquisitions accounted for \$3,133,000 of the increase. In addition, administrative cost related to the start up of Superior Precious metals, Superior Estate Buyers, American Gold and Silver Exchange and the opening of our seconded pawn shop totaled \$408,000. Depreciation and amortization increased by \$142,628, or 128.2%, during 2007 due to additional assets being purchased through our recent acquisitions. The increase in interest expense was due to the additional debt related to the Superior acquisition.

The loss from discontinued operations was the result of the closing of our pay day loan stores.

Comparison of the Years ended December 31, 2006 and 2005

Revenues increased by \$8,443,335, or 23.7%, in 2006. This increase was primarily the result of a \$5,564,000, or 53.6% increase in the sale of precious metals products, a \$1,670,000, or 11.2% increase in retail jewelry sales, and a \$1,113,000, or 23.3% increase in wholesale jewelry sales. These increases were the result of a nation-wide improvement in the retail environment, a 23.0% price increase in gold products and a 5% price increase in diamonds and other jewelry products. Pawn and pay day loan service fees increased by \$94,000 in 2006 due to increased loans in the three pay day loan stores opened in 2005. Cost of goods as a percentage of sales increased from 82.4% in 2005 to 84.4% in 2006 and gross margins decreased from 17.6% in 2005 to 15.6% in 2006. These changes were due to the increase in the precious metals sales volume as a percentage of total sales and the increase in the cost of gold products.

Selling, general and administrative expenses increased by \$420,683, or 7.9%. This increase was primarily due to an increase in staff \$294,927 and higher advertising cost \$130,944. The increase in staff was necessary to maintain a high level of customer service as sales increased. The increase in advertising was necessary in order to attract new customers in our local markets. Interest expense increased \$117,525 due to an increase in debt outstanding during the year and higher interest rates.

Historically, changes in the market prices of precious metals have had a significant impact on both revenues and cost of sales in the rare coin and precious metals segments in which we operate. It is expected that due to the commodity nature of these products, future price changes for precious metals will continue to be indicative of our performance in these business segments. Changes in sales and cost of sales in the retail and wholesale jewelry segments are primarily influenced by the national economic environment. It is expected that this trend will continue in the future due to the nature of these products.

Liquidity and Capital Resources

We expect capital expenditures to total approximately \$500,000 during the next twelve months. It is anticipated that these expenditures will be funded from working capital and our credit facility. As of December 31, 2007 there were no commitments outstanding for capital expenditures.

In the event of significant growth in retail and or wholesale jewelry sales, the demand for additional working capital will expand due to a related need to stock additional jewelry inventory and increases in wholesale accounts receivable. Historically, vendors have offered us extended payment terms to finance the need for jewelry inventory growth and our management believes that we will continue to do so in the future. Any significant increase in wholesale accounts receivable will be financed under our bank credit facility.

Our ability to finance our operations and working capital needs are dependent upon management's ability to negotiate extended terms or refinance its debt. We have historically renewed, extended or replaced short-term debt as it matures and management believes that we will be able to continue to do so in the near future.

From time to time, we have adjusted our 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 our investments in marketable securities may be liquidated in order to meet unforeseen working capital requirements.

In December 2005, we entered into a revolving credit facility with Texas Capital Bank, N.A., which currently permits borrowings up to a maximum principal amount of \$4.3 million. Borrowings under the revolving credit facility are collateralized by a general security interest in substantially all of our assets (other than the assets of Superior). As of December 31, 2007, approximately \$4.2 million was outstanding under the term loan and revolving credit facility. If we were to default under the terms and conditions of the revolving credit facility, Texas Capital Bank would have the right to accelerate any indebtedness outstanding and foreclose on our assets in order to satisfy our indebtedness. Such a foreclosure could have a material adverse effect on our business, liquidity, results of operations and financial position.

Upon the consummation of our acquisition of Superior, and after the exchange by Stanford of \$8.4 million of Superior debt for shares of Superior common stock, Superior amended and restated its credit facility with Stanford. The amended and restated commercial loan and security agreement, which we refer to as the loan agreement, decreased the available credit line from \$19.89 million to \$11.5 million, reflecting the \$8.4 million debt exchange. Interest on the outstanding principal balance will continue to accrue at the prime rate, as reported in the Wall Street Journal or, during an event of default, at a rate 5% greater than the prime rate as so reported.

The new credit facility is split into two revolving loans of \$5 million and \$6.5 million. Loan proceeds can only be used for customer loans consistent with specified loan policies and procedures and for permitted inter-company transactions. Permitted inter-company transactions are loans or dividends paid to us or our other subsidiaries. We guaranteed the repayment of these permitted inter-company transactions pursuant to a secured guaranty in favor of Stanford. In connection with the secured guarantee, Stanford and Texas Capital Bank, N.A., our primary lender, entered into an intercreditor agreement with us, and we entered into a subordination agreement with Superior, both of which subordinate Stanford's security interests and repayment rights to those of Texas Capital Bank. As of December 31, 2007, approximately \$6.7 million was outstanding under the revolving credit facility.

The new credit facility matures on May 1, 2011, provided that in case any of several customary events of default occurs, Stanford may declare the entire principal amount of both loans due immediately and take possession and dispose of the collateral described below. An event of default includes, among others, the following events: failure to make a payment when due under the loan agreement; breach of a covenant in the loan agreement or any related agreement; a representation or warranty made in the loan agreement or related agreements is materially incorrect; a default in repayment of borrowed money to any person; a material breach or default under any material contract; certain bankruptcy or insolvency events; and a default under a third-party loan. Superior is obligated to repay the first revolving loan from the proceeds of the inventory or other collateral purchased with the proceeds of the loan.

The loans are secured by a first priority security interest in substantially all of Superior's assets, including inventory, accounts receivable, promissory notes, books and records and insurance policies, and the proceeds of the foregoing. In addition, pursuant to the secured guaranty and intercreditor arrangements described above, Stanford will have a second-order security interest in all of our accounts and inventory.

The loan agreement includes a number of customary covenants applicable to Superior, including, among others: punctual payments of principal and interest under the credit facility; prompt payment of taxes, leases and other indebtedness; maintenance of corporate existence, qualifications, licenses, intellectual property rights, property and assets; maintenance of satisfactory insurance; preparation and delivery of financial statements for us and separately for Superior in accordance with generally accepted accounting principles, tax returns and other financial information; inspection of offices and collateral; notice of certain events and changes; use of proceeds; notice of governmental orders which may have a material adverse effect, SEC filings and stockholder communications; maintenance of property and collateral; and payment of Stanford expenses.

In addition, Superior has agreed to a number of negative covenants in the loan agreement, including, among others, covenants not to: create or suffer a lien or other encumbrance on any collateral, subject to customary exceptions; incur, guarantee or otherwise become liable for any indebtedness, subject to customary exceptions; acquire indebtedness of another person, subject to customary exceptions and permitted inter-company transactions; issue or acquire any shares of its capital stock; pay dividends other than permitted inter-company transactions or specified quarterly dividends, or directors' fees; sell or abandon any collateral except in the ordinary course of business or consolidate or merge with another entity; enter into affiliate transactions other than in the ordinary course of business on fair terms or permitted inter-company transactions; create or participate in any partnership or joint venture; engage in a new line of business; pay principal or interest on subordinate debt except as authorized by the credit facility; or make capital expenditures in excess of \$100,000 per fiscal year.

On October 17, 2007, we closed on the purchase of our new headquarters location. As a result, we assumed a new loan with a remaining principal balance of \$2,441,922 and an interest rate of 6.70%. The loan has required monthly payments of \$20,192.00 with the final payment due on August 1, 2016.

| Contractual Cash Obligations | Total | Payments due by period | | | |
|-----------------------------------|----------------------|------------------------|---------------------|---------------------|---------------------|
| | | 2008 | 2009 - 2010 | 2011 - 2012 | Thereafter |
| Notes payable | \$ 187,467 | \$ 187,467 | \$ — | \$ — | \$ — |
| Long-term debt and capital leases | 13,991,532 | 501,631 | 4,306,121 | 6,906,337 | 2,277,443 |
| Federal income taxes | 48,023 | 48,023 | — | — | — |
| Operating Leases | 3,488,490 | 771,529 | 1,518,477 | 1,150,244 | 48,240 |
| Total | \$ 17,715,512 | \$ 1,508,650 | \$ 5,824,598 | \$ 8,056,581 | \$ 2,325,683 |

In addition, we estimate that we will pay approximately \$950,000 in interest during the next twelve months.

ITEM 7A. QUALITATIVE AND QUANTITATIVE DISCLOSURES ABOUT MARKET RISK.

Market Risk

The following discussion about our market risk disclosures involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements. We are exposed to market risk related to changes in interest rate and precious metal values. We also are exposed to regulatory risk in relation to our payday loans. We do not use derivative financial instruments.

Our earnings and financial position may be affected by changes in precious metal values and the resulting impact on pawn lending and jewelry sales. The proceeds of scrap sales and our ability to liquidate excess jewelry inventory at an acceptable margin are dependent upon gold values. The impact on our financial position and results of operations of a hypothetical change in precious metal values cannot be reasonably estimated.

ITEM 8. FINANCIAL STATEMENTS.

- (a) Financial Statements (see pages 26 - 44 of this report).

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None.

ITEM 9A. CONTROLS AND PROCEDURES.

Disclosure Controls and procedures

An evaluation was performed under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this annual report. Our disclosure controls and procedures are designed to ensure that information required to be disclosed by us in the reports we file or submit under the Securities Exchange Act of 1934, as amended, is (1) recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and (2) accumulated and communicated to our management, including our Chief Executive Officer, to allow timely decisions regarding required disclosure. Based on that evaluation, our management, including our Chief Executive Officer and our Chief Financial Officer, concluded that our disclosure controls and procedures were effective.

Management's Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting as such term is defined in Exchange Act Rule 13a-15(f). The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, management assessed the effectiveness of our internal control over financial reporting as of December 31, 2007. In making its assessment of internal control over financial reporting, management used the criteria described in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. In conjunction with our auditors, management identified five material weaknesses in the Company's internal control over financial reporting. A material weakness is a significant deficiency, or a combination of significant deficiencies which when aggregated, results in there being more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis by employees in the normal course of their assigned functions. As a result of these material weaknesses, we concluded that the Company's internal control over financial reporting was not effective as of December 31, 2007 based on the criteria in Internal Control — Integrated Framework. We are taking steps to address these material weaknesses which could possibly have led to a material misstatement in our financial statements if not detected and corrected.

We identified two material weaknesses in our internal controls over cash. The Controller performs the bank reconciliation. There is no review of the bank reconciliation to ensure that cash per the bank statement agrees to the general ledger and that there are no long-term outstanding reconciling items. Management has agreed that the CFO will review and approve the bank statements and reconciliations to remediate the control weakness. The second material weakness in the cash area relates to internal controls around wire transfers. The CFO initiates and releases most wire transfers without prior written or documented approval. Management has agreed to initiate controls whereby the President or a Vice-President will be required to approve all wire transfers.

We also identified a material weakness in accounts payable. The quarterly accrual is not reviewed for accuracy nor is there a documented approval of the accounts payable accrual. There is a risk that liabilities may be understated for the

period reported. Management has agreed to take corrective action to include a review of accrued liabilities by someone other than the person performing the accrual.

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We also identified a material weakness in the approval process around changes made to the general ledger structure. During the reporting period there has been incomplete and undocumented supervisory review of changes and additions made to the general ledger accounts. Additionally, a material weakness was detected in the closing process. The review and approval of the major balance sheet account reconciliations are undocumented during the closing process. Management has agreed to take corrective action to improve review procedures for changes made to the general ledger account structure, reconciliations and closing procedures. Management has also agreed to document supervisory review and approval of these general ledger account changes, account reconciliations and closing procedures.

This Annual Report on Form 10-K does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit the Company to provide only management's report in this Annual Report on Form 10-K.

Changes in Internal Control over Financial Reporting

For the year ended December 31, 2007, there have been no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934) that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION.

None.

PART III

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES. (*)

(*) The information required by Item 14 is or will be set forth in the definitive proxy statement relating to the 2008 Annual Meeting of Stockholders of DGSE Companies, Inc., which is to be filed with the Securities and Exchange Commission pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended. This definitive proxy statement relates to a meeting of stockholders involving the election of directors and the portions therefrom required to be set forth in this Form 10-K by Item 14 are incorporated herein by reference pursuant to General Instruction G(3) to Form 10-K.

PART IV**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

| (a) Exhibits | | | | | | |
|---------------------|---|---------------------|----------------------------------|-------------|----------------------------|--------------------|
| Exhibit No. | Description | Filed Herein | Incorporated by Reference | Form | Date Filed with SEC | Exhibit No. |
| 2.1 | Amended and Restated Agreement and Plan of Merger and Reorganization, dated as of January 6, 2007 | | × | 8-K | January 9, 2007 | 2.1 |
| 2.2 | Limited Joinder Agreement, dated as of January 6, 2007 | | × | 8-K | January 9, 2007 | 2.9 |
| 3.1 | Articles of Incorporation dated September 17, 1965 | | × | 8-A12G | June 23, 1999 | 3.1 |
| 3.2 | Certificate of Amendment to Articles of Incorporation, dated October 14, 1981 | | × | 8-A12G | June 23, 1999 | 3.2 |
| 3.3 | Certificate of Resolution, dated October 14, 1981 | | × | 8-A12G | June 23, 1999 | 3.3 |
| 3.4 | Certificate of Amendment to Articles of Incorporation , dated July 15, 1986 | | × | 8-A12G | June 23, 1999 | 3.4 |
| 3.5 | Certificate of Amendment to Articles of Incorporation, dated August 23, 1998 | | × | 8-A12G | June 23, 1999 | 3.5 |
| 3.6 | Certificate of Amendment to Articles of Incorporation, dated June 26, 1992 | | × | 8-A12G | June 23, 1999 | 3.6 |
| 3.7 | Certificate of Amendment to Articles of Incorporation, dated June 26, 2001 | | × | 8-K | July 3, 2001 | 1.0 |
| 3.8 | Certificate of Amendment to Articles of Incorporation, dated May 22, 2007 | | x | 8-K | May 31, 2007 | 3.1 |
| 3.9 | By-laws, dated March 2, 1992 | | × | 8-A12G | June 23, 1999 | 3.7 |
| 4.1 | | | × | S-4 | | 4.1 |

Specimen Common Stock
Certificate

January 6,
2007

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| | | | | | |
|------|--|---|--------|-----------------|------|
| 10.1 | Renewal, Extension And Modification Agreement dated January 28, 1994, by and among DGSE Corporation and Michael E. Hall And Marian E. Hall | × | 10-KSB | March 1995 | 10.2 |
| 10.2 | Lease Agreement dated June 2, 2000 by and between SND Properties and Charleston Gold and Diamond Exchange, Inc. | × | 10-KSB | March 29, 2001 | 10.1 |
| 10.3 | Lease agreement dated October 5, 2004 by and between Beltline Denton Road Associates and Dallas Gold & Silver Exchange | × | 10-K | April 15, 2005 | 10.2 |
| 10.4 | Lease agreement dated December 1, 2004 by and between Stone Lewis Properties and Dallas Gold & Silver Exchange | × | 10-K | April 15, 2005 | 10.3 |
| 10.5 | Lease agreement dated November 18, 2004 by and between Hinkle Income Properties LLC and American Pay Day Centers, Inc. | × | 10-K | April 15, 2005 | 10.4 |
| 10.6 | Lease Agreement dated January 17, 2005 by and between Belle-Hall Development Phase III Limited Partnership and DGSE Companies, Inc. | × | S-4 | January 6, 2007 | 10.6 |
| 10.7 | Sale agreement dated executed July 5, 2007 by and between DGSE Companies, Inc. and Texas Department of Transportation | × | 8-K | July 11, 2007 | 10.1 |
| 10.8 | Purchase agreement dated July 5, 2007 by and between DGSE Companies, Inc. and 11311 Reeder Road Holdings, LP | × | 8-K | July 11, 2007 | 10.2 |

| | | | | | |
|------|---|---|-------|--------------------|------|
| 10.9 | Loan Agreement, dated as of December 22, 2005, between DGSE Companies, Inc. and Texas Capital Bank, N.A. | × | 8-K/A | August 17, 2006 | 10.1 |
|------|---|---|-------|--------------------|------|

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| | | | | | |
|-------|--|---|-----|-----------------|------|
| 10.10 | Third Amendment to Loan Agreement, dated as of May 10, 2007, by and between DGSE Companies, Inc. and Texas Capital Bank, N.A. | × | 8-K | May 9, 2007 | 3.0 |
| 10.11 | Support Agreement, DGSE stockholders, dated as of January 6, 2007 | × | 8-K | January 9, 2007 | 99.1 |
| 10.12 | Securities Exchange Agreement, dated as of January 6, 2007 | × | 8-K | January 9, 2007 | 99.2 |
| 10.13 | Warrant to DiGenova, issued January 6, 2007 | × | 8-K | January 9, 2007 | 99.3 |
| 10.14 | Support Agreement, Superior stockholders, dated as of January 6, 2007 | × | 8-K | January 9, 2007 | 99.5 |
| 10.15 | Asset purchase agreement, dated May 9, 2007, by and between DGSE Companies, Inc. and Eules Gold & Silver, Inc. | × | 8-K | May 9, 2007 | 1.0 |
| 10.16 | Subordinated Promissory Note dated May 9, 2007 | × | 8-K | May 9, 2007 | 2.0 |
| 10.17 | Registration Rights Agreement with Stanford International Bank Ltd., dated as of May 30, 2007 | × | 8-K | May 31, 2007 | 99.1 |
| 10.18 | Corporate Governance Agreement with Dr. L.S. Smith and Stanford International Bank Ltd., dated as of May 30, 2007 | × | 8-K | May 31, 2007 | 99.2 |
| 10.19 | Escrow Agreement with American Stock Transfer & Trust Company and Stanford International Bank Ltd., as stockholder agent, dated as of May 30, 2007 | × | 8-K | May 31, 2007 | 99.3 |
| 10.20 | Form of Warrants | × | 8-K | May 31, 2007 | 99.4 |

| | | | | | |
|-------|--|---|-----|--------------|------|
| 10.21 | Amended and Restated Commercial Loan and Security Agreement, by and between Superior Galleries Inc. and Stanford International Bank Ltd., dated as of May 30, 2007 | × | 8-K | May 31, 2007 | 99.5 |
|-------|--|---|-----|--------------|------|

| | | | | | |
|-------|--|---|-----|--------------|------|
| 10.22 | Employment Agreement with L.S. Smith, dated as of May 30, 2007 | × | 8-K | May 31, 2007 | 99.6 |
| 10.23 | Employment Agreement with William H. Oyster, dated as of May 30, 2007 | × | 8-K | May 31, 2007 | 99.7 |
| 10.24 | Employment Agreement with John Benson, dated as of May 30, 2007 | × | 8-K | May 31, 2007 | 99.8 |
| 31.1 | Certification pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 implementing Section 302 of the Sarbanes-Oxley Act of 2002 by Dr. L.S. Smith | × | | | |
| 31.2 | Certification pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 implementing Section 302 of the Sarbanes-Oxley Act of 2002 by John Benson | × | | | |
| 32.1 | Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 by Dr. L.S. Smith | × | | | |
| 32.2 | Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 by John Benson | × | | | |

(b) Reports on Form 8-K :

None.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

DGSE Companies, Inc.

By: /s/ L. S. Smith

Dated: March 31, 2008

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

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

By: /s/ L. S. Smith

Dated: March 31, 2008

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

By: /s/ W. H. Oyster

Dated: March 31, 2008

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

By: /s/ John Benson

Dated: March 31, 2008

John Benson
Chief Financial Officer
(Principal Accounting Officer)

By: /s/ William P. Cordeiro

Dated: March 31, 2008

Director

By: /s/ Craig Allan-Lee

Dated: March 31, 2008

Director

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By: /s/ Mitch Stoltz

Dated: March 31, 2008

Director

By: /s/ David Rector

Dated: March 31, 2008

Director

By: /s/ Richard Gozia

Dated: March 31, 2008

Director

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and
Shareholders of DGSE Companies, Inc.

We have audited the accompanying consolidated balance sheets of DSGE Companies, Inc. and its subsidiaries (the "Company") as of December 31, 2007 and 2006, and the related consolidated statements of operations, shareholders' equity and comprehensive income, and cash flows for the years ended December 31, 2007, 2006, and 2005. These consolidated 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 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. We have not been engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly we express no such opinion. 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 financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2007 and 2006, and the consolidated results of operations and its cash flows for the years ended December 31, 2007, 2006, and 2005 in conformity with accounting principles generally accepted in the United States of America.

/s/ Cornwell Jackson
Plano, Texas
March 31, 2008

DGSE COMPANIES, INC. AND SUBSIDIARIES**CONSOLIDATED BALANCE SHEETS**

| | December 31, | |
|---|---------------------|-------------------|
| ASSETS | 2007 | 2006 |
| Current Assets: | | |
| Cash and cash equivalents | \$ 536,548 | \$ 1,210,282 |
| Trade receivables | 3,792,474 | 1,053,454 |
| Auction advances | 747,000 | — |
| Inventories | 12,975,782 | 7,796,028 |
| Prepaid expenses | 459,486 | 192,379 |
| Prepaid federal income tax | 59,341 | 97,472 |
| Total current assets | 18,570,631 | 10,349,615 |
| Marketable securities - available for sale | 61,769 | 57,879 |
| Property and equipment, net | 4,193,869 | 1,024,405 |
| Deferred income taxes | 1,805,205 | 7,152 |
| Goodwill | 8,952,181 | 837,117 |
| Intangible assets | 2,521,340 | — |
| Other long-term receivable | 444,383 | — |
| Other assets | 309,836 | 869,398 |
| | \$ 36,859,214 | \$ 13,145,566 |
| LIABILITIES | | |
| Current Liabilities: | | |
| Notes payable | \$ 187,467 | \$ 183,708 |
| Current maturities of long-term debt | 501,631 | 259,273 |
| Accounts payable - trade | 1,069,194 | 828,323 |
| Accrued expenses | 1,018,003 | 721,305 |
| Customer deposits | 315,437 | 171,912 |
| Total current liabilities | 3,091,732 | 2,164,521 |
| Long-term debt, less current maturities | 13,489,901 | 4,303,685 |
| | 16,581,633 | 6,468,206 |
| STOCKHOLDERS' EQUITY | | |
| Common stock, \$.01 par value; 30,000,000 shares authorized; 9,490,357 and 4,913,290 shares issued and outstanding at the end of each period in 2007 and 2006 | 94,904 | 49,133 |
| Additional paid-in capital | 18,473,234 | 5,708,760 |
| Accumulated other comprehensive loss | (97,288) | (132,245) |
| Retained earnings | 1,806,731 | 1,051,712 |
| | 20,277,581 | 6,677,360 |
| | \$ 36,859,214 | \$ 13,145,566 |

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

DGSE COMPANIES, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF OPERATIONS**

| | Years ended December 31, | | |
|---|--------------------------|---------------|---------------|
| | 2007 | 2006 | 2005 |
| Revenue | | | |
| Sales | \$ 62,410,392 | \$ 43,668,973 | \$ 35,319,133 |
| Consumer loan service charges | 306,413 | 187,772 | 241,355 |
| Management fees | 250,000 | — | — |
| | 62,966,805 | 43,856,745 | 35,560,488 |
| Costs and expenses | | | |
| Cost of goods sold | 51,730,886 | 36,809,910 | 29,088,545 |
| Selling, general and administrative expenses | 9,725,448 | 5,529,314 | 5,154,514 |
| Depreciation and amortization | 253,887 | 111,259 | 126,149 |
| | 61,710,221 | 42,450,483 | 34,369,208 |
| Operating income | 1,256,584 | 1,406,262 | 1,191,280 |
| Other (income) expense | | | |
| Other (income) expense | (575,813) | (16,534) | (18,038) |
| Interest expense | 675,199 | 408,269 | 290,744 |
| Earnings before income taxes | 1,157,198 | 1,014,527 | 918,574 |
| Income tax expense | 281,234 | 348,188 | 328,049 |
| Net earnings from continuing operations | 875,964 | 666,339 | 590,525 |
| Discontinued operations: | | | |
| Loss from discontinued operations (less applicable income tax benefit of \$12,622, \$28,382 and \$58,507, respectively) | 39,315 | 55,094 | 105,333 |
| Loss on disposal of discontinued operations (less applicable income tax benefit of \$26,208, \$0 and \$0, respectively) | 81,630 | — | — |
| Net earnings | \$ 755,019 | \$ 611,245 | \$ 485,192 |
| Earnings per common share | | | |
| Basic | | | |
| From continuing operations | \$.12 | \$.14 | \$.12 |
| From discontinued operations | (.02) | (.02) | (.02) |
| Net earnings per common share | \$.10 | \$.12 | \$.10 |
| Diluted | | | |
| From continuing operations | \$.11 | \$.13 | \$.12 |
| From discontinued operations | (.01) | (.01) | (.02) |
| Net earnings per common share | \$.09 | \$.12 | \$.10 |

| | | | |
|---|-----------|-----------|-----------|
| Weighted average number of common shares: | | | |
| Basic | 7,507,579 | 4,913,290 | 4,913,290 |
| Diluted | 8,281,887 | 5,006,909 | 5,037,073 |

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

*DGSE COMPANIES, INC. AND SUBSIDIARIES***CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31,**

| | Common Stock | | Additional Paid-in Capital | Retained Earnings | Other | Total Stockholder's Equity |
|--|--------------|-----------|----------------------------------|--------------------------|-----------------------------------|----------------------------------|
| | Shares | Amount | | (Accumulated Deficit) | Comprehensive Income (Loss) | |
| Balance at January 1, 2005 | 4,913,290 | \$ 49,133 | \$ 5,708,760 | \$ (44,725) | \$ (122,582) | \$ 5,590,586 |
| Net earnings | | | | 485,192 | | 485,192 |
| Unrealized loss on marketable securities, net of tax | | | | | (4,670) | (4,670) |
| Balance at December 31, 2005 | 4,913,290 | \$ 49,133 | \$ 5,708,760 | \$ 440,467 | \$ (127,252) | \$ 6,071,128 |
| Net earnings | | | | 611,245 | | 611,245 |
| Unrealized loss on marketable securities, net of tax | | | | | (4,993) | (4,993) |
| Balance at December 31, 2006 | 4,913,290 | \$ 49,133 | \$ 5,708,760 | \$ 1,051,712 | \$ (132,245) | \$ 6,677,360 |
| Net earnings | | | | 755,019 | | 755,019 |
| Unrealized gain on marketable securities, net of tax | | | | | 34,957 | 34,957 |
| Acquisition of Superior | 3,669,067 | 36,691 | 12,593,172 | | | 12,629,863 |
| Conversion of warrants | 908,000 | 9,080 | 142,485 | | | 151,565 |
| Stock based compensation | | | 28,817 | | | 28,817 |
| Balance at December 31, 2007 | 9,490,357 | \$ 94,904 | \$ 18,473,234 | \$ 1,806,731 | \$ (97,288) | \$ 20,277,581 |

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

DGSE COMPANIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31,

| | 2007 | 2006 | 2005 |
|--|-------------|--------------|--------------|
| Cash flows from operating activities | | | |
| Net earnings | \$ 755,019 | \$ 611,245 | \$ 485,192 |
| Adjustments to reconcile net earnings to net cash provided by operating activities | | | |
| Depreciation and amortization | 253,887 | 139,395 | 145,337 |
| Deferred taxes | (31,692) | (3,801) | 21,832 |
| Gain on sale of marketable securities | (3,890) | — | (3,845) |
| Loss on discontinued operations | 120,945 | — | — |
| Gain on sale of building | (579,447) | — | — |
| (Increase) decrease in operating assets and liabilities | | | |
| Trade receivables | (3,345,559) | (317,694) | 183,578 |
| Inventories | (928,838) | (225,908) | (778,735) |
| Prepaid expenses and other current assets | (70,810) | 23,181 | (53,577) |
| Change in other long term assets | 181,855 | (11,826) | 182 |
| Accounts payable and accrued expenses | (695,689) | 179,081 | 266,360 |
| Change in customer deposits | 24,712 | (34,408) | 139,147 |
| Federal income taxes payable | 38,131 | (111,392) | (132,290) |
| Net cash provided by (used in) operating activities | (4,281,376) | 247,793 | 273,131 |
| Cash flows from investing activities | | | |
| Pawn loans made | (714,209) | (485,595) | (602,987) |
| Pawn loans repaid | 380,060 | 417,124 | 454,707 |
| Recovery of pawn loan principal through sale of forfeited collateral | 204,121 | 100,960 | 248,695 |
| Pay day loans made | (164,289) | (274,973) | (177,775) |
| Pay day loans repaid | 125,982 | 195,534 | 112,210 |
| Purchase of property and equipment | (3,780,554) | (42,058) | (285,456) |
| Deal cost for Superior Galleries acquisition | (375,280) | (569,782) | — |
| Acquisition of Eules Gold & Silver | (600,000) | — | — |
| Proceeds from sale of discontinued operations | 77,496 | — | — |
| Proceeds from sale of building | 924,742 | — | — |
| Proceeds from sale of marketable securities | 396 | — | 4,226 |
| Net cash used in investing activities | (3,921,535) | (658,790) | (246,380) |
| Cash flows from financing activities | | | |
| Proceeds from notes issue | 6,991,578 | 1,247,350 | 8,371,525 |
| Mortgage on new corporate office and store location | 2,441,922 | — | — |
| Issuance of common stock | 78,363 | — | — |
| Repayments of notes payable | (1,982,686) | (668,905) | (7,670,339) |
| Net cash provided by financing activities | 7,529,177 | 578,445 | 701,186 |
| Net increase (decrease) in cash and cash equivalents | (673,734) | 167,448 | 727,937 |
| Cash and cash equivalents at beginning of period | 1,210,282 | 1,042,834 | 314,897 |
| Cash and cash equivalents at end of period | \$ 536,548 | \$ 1,210,282 | \$ 1,042,834 |

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

DGSE COMPANIES, INC. AND SUBSIDIARIES**Consolidated Statements of Cash Flows** *(Continued)***Supplemental disclosures:**

| | 2007 | | 2006 | | 2005 |
|--------------------------------|-------------|----|-------------|----|-------------|
| Cash paid during the year for: | | | | | |
| Interest | \$ 572,592 | \$ | 378,562 | \$ | 300,866 |
| Income taxes | \$ 50,000 | \$ | 435,000 | \$ | 385,000 |

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

DGSE Companies, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2007, 2006 and 2005

Note 1 - Summary of Accounting Policies and Nature of Operations

A summary of the significant accounting policies applied in the preparation of the accompanying consolidated financial statements follows:

Principles of Consolidation and Nature of Operations

DGSE Companies, Inc. and its subsidiaries (the "Company"), sell jewelry and bullion products to both retail and wholesale customers throughout the United States through its facilities in Dallas and Eules, Texas, Mt. Pleasant, South Carolina, Beverly Hills California and through its internet sites.

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and include the accounts of the Company and its subsidiaries. All material intercompany transactions and balances have been eliminated.

On July 13, 2007, we sold the loan balances from our American Pay Day Center locations and discontinued operations in those locations. As a result of this disposition, the Consolidated Financial Statements and related notes have been reclassified to present the results of the American Pay Day Center locations as discontinued operations.

Cash and Cash Equivalents

For purposes of the statements of cash flows, the Company considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

Investments in Marketable Equity Securities

Marketable equity securities have been categorized as available-for-sale and carried at fair value. Unrealized gains and losses for available-for-sale securities are included as a component of shareholders' equity net of tax until realized. Realized gains and losses on the sale of securities are based on the specific identification method. The Company continually reviews its investments to determine whether a decline in fair value below the cost basis is other than temporary. If the decline in the fair values is judged to be other than temporary, the cost basis of the security is written down to fair value and the amount of the write-down is included in the consolidated statements of operations.

Inventory

Jewelry and other inventory is valued at lower-of-cost-or-market (specific identification). Bullion inventory is valued at lower-of-cost-or-market (average cost).

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are being provided on the straight-line method over periods of three to thirty years. Machinery and equipment under capital leases are amortized on the straight-line method over the life of the lease. Expenditures for repairs and maintenance are charged to expense as incurred.

Goodwill

Effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets*. Under that pronouncement, goodwill is not being amortized but is subject to periodic tests to determine the amount of impairment, if any, to be reflected during the period.

Impairment of Long-Lived Assets

The Company assesses the recoverability of its long-lived assets (including intangible assets) based on their current and anticipated future undiscounted cash flows. An impairment occurs when the discounted cash flows (excluding interest) do not exceed the carrying amount of the asset. The amount of the impairment loss is the difference between the carrying amount of the asset and its estimated fair value.

DGSE Companies, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2007, 2006 and 2005

Note 1 - Summary of Accounting Policies and Nature of Operations - *continued*

Financial Instruments

The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, accounts receivable, marketable securities, short-term debt, accounts payable and accrued expenses approximate fair value because of the immediate or short-term maturity of these consolidated financial instruments. The carrying amount reported for long-term debt approximates fair value because substantially all of the underlying instruments have variable interest rates which repriced frequently or the interest rates approximate current market rates.

Advertising Costs

Advertising costs are expensed as incurred and amounted to \$1,442,723, \$823,106 and \$719,080 for 2007, 2006 and 2005, respectively.

Accounts Receivable

The Company records trade receivables when revenue is recognized. No product has been consigned to customers. The Company's allowance for doubtful accounts is primarily determined by review of specific trade receivables. Those accounts that are doubtful of collection are included in the allowance. These provisions are reviewed to determine the adequacy of the allowance for doubtful accounts. Trade receivables are charged off when there is certainty as to their being uncollectible. Trade receivables are considered delinquent when payment has not been made within contract terms. As of December 31, 2007, the Company had a recorded allowance amount of \$700,075 which had been recorded by Superior prior to us acquiring them. The balance of the Company's trade receivables is net of the allowance amount.

Pawn loans receivable in the amount of \$263,856 and \$95,422 as of December 31, 2007 and 2006, respectively, are included in the Consolidated Balance Sheets caption trade receivables. The related pawn service charges receivable in the amount of \$63,532 and \$33,998 as of December 31 2007 and 2006, respectively, are also included in the Consolidated Balance Sheets caption trade receivables.

Income Taxes

Deferred tax liabilities and assets are recognized for the expected future tax consequences of events that have been included in the consolidated financial statements or tax returns. Under this method, deferred tax liabilities and assets are determined based on the difference between the consolidated financial statements and tax basis of assets and liabilities.

Revenue Recognition

The Company generates revenue from wholesale and retail sales of rare coins, precious metals bullion and second-hand jewelry. The recognition of revenue varies for wholesale and retail transactions and is, in large part, dependent on the type of payment arrangements made between the parties. We recognize sales on an F.O.B. shipping point basis.

The Company sells rare coins to other wholesalers/dealers within its industry on credit, generally for terms of 15 to 60 days, but in no event greater than one year. The Company grants credit to new dealers based on extensive credit evaluations and for existing dealers based on established business relationships and payment histories. The Company generally does not obtain collateral with which to secure its accounts receivable when the sale is made to a dealer. The Company maintains reserves for potential credit losses based on an evaluation of specific receivables, offset rights and the Company's historical experience related to credit losses.

The Company also sells rare coins to retail customers on credit, generally for terms of 30 to 60 days, but in no event greater than one year. The Company grants credit to retail customers based on extensive credit evaluations and for existing retail customers based on established business relationships and payment histories. When a retail customer is granted credit, the Company generally collects a payment of 25% of the sales price, establishes a payment schedule for the remaining balance and holds the merchandise as collateral as security against the customer's receivable until all amounts due under the credit arrangement are paid in full. If the customer defaults in the payment of any amount when due, the Company may declare the customer's obligation in default, liquidate the collateral in a commercially reasonable manner using such proceeds to extinguish the remaining balance and disburse any amount in excess of the remaining balance to the customer.

Under this retail arrangement, revenues are recognized when the customer agrees to the terms of the credit and makes the initial payment. The Company's has a limited-in-duration money back guaranty policies (as discussed below).

In limited circumstances, the Company exchanges merchandise for similar merchandise and/or monetary consideration with both dealers and retail customers, for which the Company recognizes revenue in accordance with APB No. 29, "*Accounting for Non-monetary Transactions.*" When the Company exchanges merchandise for similar merchandise and there is no monetary component to the exchange, the Company does not recognize any revenue. Instead, the basis of the merchandise relinquished becomes the basis of the merchandise received, less any indicated impairment of value of the merchandise relinquished. When the Company exchanges merchandise for similar merchandise and there is a monetary component to the exchange, the Company recognizes revenue to the extent of monetary assets received and determines the cost of sale based on the ratio of monetary assets received to monetary and non-monetary assets received multiplied by the cost of the assets surrendered.

The Company has a return policy (money-back guarantee). The policy covers retail transactions involving graded rare coins only. Customers may return graded rare coins purchased within 7 days of the receipt of the rare coins for a full refund as long as the rare coins are returned in exactly the same condition as they were delivered. In the case of rare coin sales on account, customers may cancel the sale within 7 days of making a commitment to purchase the rare coins. The receipt of a deposit and a signed purchase order evidences the commitment. Any customer may return a coin if they can demonstrate that the coin is not authentic, or there was an error in the description of a graded coin.

Revenues from the sale of consigned goods are recognized as commission income on such sale if the Company is acting as an agent for the consignor. If in the process of selling consigned goods, the Company makes an irrevocable payment to a consignor for the full amount due on the consignment and the corresponding receivable from the buyer(s) has not been collected by the Company at that payment date, the Company records that payment as a purchase and the sale of the consigned good(s) to the buyer as revenue as the Company has assumed all collection risk.

The Company's auction business generates revenue in the form of commissions charged to buyers and sellers of auction lots. Auction commissions include buyers' commissions, sellers' commissions, and buyback commissions, each of which are calculated based on a percentage of the hammer price.

Buyers' and sellers' commissions are recognized upon the confirmation of the identification of the winning bidders. Funds charged to winning bidders include the hammer price plus the commission. Only the commission portion of the funds received by winning bidders is recorded as revenue.

Buyback commissions represent an agreed upon rate charged by the Company for goods entered in the auction and not sold. Goods remain unsold when an auction lot does not meet the consignor reserve, which is the minimum sales price as determined prior to auction, and when items sold at auction are returned subsequent to the winning bidder taking possession. Returns from winning bidders are very limited and primarily occur when a rare coin sold auction has an error in its description in which the winner bidder relied upon-to purchase the item. Buyback commission is recognized along with sellers' commission or at the time an item is returned.

Pawn loans ("loans") are made with the collateral of tangible personal property for one month with an automatic 60-day extension period. Pawn service charges are recorded at the time of redemption at the greater of \$15 or the actual interest accrued to date. If the loan is not repaid, the principal amount loaned plus accrued interest (or the fair value of the collateral, if lower) becomes the carrying value of the forfeited collateral ("inventories") which is recovered through sales to customers.

As of December 31, 2007, based on subsequent collections and operating history, management estimated no allowance for discounts, returns, bad debts and other adjustments.

Direct cost of Pawn Loan Service Charge Revenue

The direct cost of pawn loan service charge revenue is included in the Consolidated Statements of Operations caption “Selling, general and administrative expenses”.

Shipping and Handling Costs

Shipping and handling costs are included in selling general and administrative expenses, and amounted to \$266,867, \$178,999 and \$155,876 for 2007, 2006 and 2005, respectively.

DGSE Companies, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2007, 2006 and 2005

Note 1 - Summary of Accounting Policies and Nature of Operations - *continued*

Earnings (Loss) Per Share

Basic earnings per common share is based upon the weighted average number of shares of common stock outstanding. Diluted earnings per share is based upon the weighted average number of common stock outstanding and, when dilutive, common shares issuable for stock options.

Comprehensive Income

The Company reports all changes in comprehensive income in the consolidated statements of changes in shareholders' equity, in accordance with the provisions of Statement of Financial Accounting Standards No. 130, *Reporting Comprehensive Income*.

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

| | Year Ended December 31, | | |
|---|--------------------------------|------------|------------|
| | 2007 | 2006 | 2005 |
| Net earnings, as reported | \$ 755,019 | \$ 611,245 | \$ 485,192 |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects | N/A | N/A | (4,554) |
| Pro forma net earnings | \$ N/A | \$ N/A | \$ 480,638 |
| Earnings per share: | | | |
| Basic - as reported | \$ 0.10 | \$ 0.12 | \$ 0.10 |
| Basic - pro forma | \$ 0.10 | \$ 0.12 | \$ 0.10 |
| Diluted - as reported | \$ 0.09 | \$ 0.12 | \$ 0.10 |
| Diluted - pro forma | \$ 0.09 | \$ 0.12 | \$ 0.10 |

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.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported

amounts of revenues, and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications were made to the prior years' consolidated financial statements to conform to the current year presentation.

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DGSE Companies, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2007, 2006 and 2005

Note 1 - Summary of Accounting Policies and Nature of Operations - *continued*

New Accounting Pronouncements

In December 2007, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards No. 160, *Noncontrolling Interests in Consolidated Financial Statements — an amendment of Accounting Research Bulletin No. 51* (“SFAS 160”), which establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 is effective for the Company beginning January 1, 2009. As the Company does not hold any noncontrolling interests, it believes the impact of adopting SFAS 160 will not have a material effect on its consolidated statement of earnings, financial condition, statement of cash flows or earnings per share.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141R, *Business Combinations* (“SFAS 141R”), which establishes principles and requirements for the reporting entity in a business combination, including recognition and measurement in the financial statements of the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree. This statement also establishes disclosure requirements to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS 141R is effective for the Company on a prospective basis for business combinations for which the acquisition date is on or subsequent to the reporting period beginning January 1, 2009. The impact of adopting SFAS 141R will depend on the nature and terms of future acquisitions, if any.

Note 2 - Concentration of Credit Risk

The Company maintains cash balances in financial institutions in excess of federally insured limits.

Note 3 - Inventories

A summary of inventories at December 31, is as follows:

| | 2007 | 2006 |
|------------|---------------|--------------|
| Jewelry | \$ 8,118,454 | \$ 7,022,453 |
| Scrap gold | 414,099 | 374,284 |
| Bullion | 486,991 | 113,867 |
| Rare coins | 3,482,248 | 235,099 |
| Other | 473,990 | 50,325 |
| Total | \$ 12,975,782 | \$ 7,796,028 |

Note 4 - Investments in Marketable Equity Securities

Marketable equity securities have been classified in the consolidated balance sheet according to management’s intent. The carrying amount of available-for-sale securities and their fair values at December 31, 2007 and 2006 are as follows:

| Cost | Gross Unrealized Losses | | Fair Value |
|------|--------------------------------|---------------------------------|------------|
| | Classified as operating losses | Classified as unrealized losses | |

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| | | | due to long-term impairment | | in other comprehensive income | | | |
|------------------------|----|-----------|--------------------------------|-------------|-------------------------------------|-----------|----|--------|
| Equity securities 2007 | \$ | 1,408,441 | \$ | (1,249,474) | \$ | (97,288) | \$ | 61,769 |
| Equity securities 2006 | \$ | 1,864,441 | \$ | (1,634,845) | \$ | (171,717) | \$ | 57,879 |

At December 31, 2007, management believes the equity shares owned in the publicly traded stocks have declined on a temporary basis as these stocks are thinly traded which results in volatile price flections that temporarily changes the fair value of the stocks. Management also believes its intent and ability to hold these investments supports the Company's position to categorize the fluctuation in value as temporary.

DGSE COMPANIES, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements - *continued*
December 31, 2007, 2006 and 2005

Note 5 - Property and Equipment

A summary of property and equipment at December 31, 2007 and 2006, is as follows:

| | 2007 | 2006 |
|--|---------------------|---------------------|
| Buildings and improvements | \$ 2,565,533 | \$ 712,239 |
| Machinery and equipment | 812,833 | 247,962 |
| Furniture and fixtures | 806,108 | 73,725 |
| | 4,184,474 | 1,033,926 |
| Less accumulated depreciation and amortization | 1,151,075 | 560,851 |
| | 3,033,399 | 473,075 |
| Land | 1,160,470 | 551,330 |
| Total Property and Equipment | \$ 4,193,869 | \$ 1,024,405 |

During 2007, we sold the land and building at which our Dallas retail store and corporate headquarters were previously located, which resulted in a net book value disposition of \$712,518. Additionally, the acquisition of Superior Galleries and the purchase of our new land and buildings for our Dallas retail store and corporate headquarters during the fourth quarter of 2007 resulted in a net addition of \$3,691,579 to property and equipment.

Note 6 - Acquisitions

Superior Galleries, Inc. On May 30, 2007, we completed our acquisition of Superior Galleries, Inc., which we refer to as Superior, pursuant to an amended and restated agreement and plan of merger and reorganization dated as of January 6, 2007, which we refer to as the merger agreement, with Superior and Stanford International Bank Ltd., then Superior's largest stockholder and its principal lender, which we refer to as Stanford, as stockholder agent for the Superior stockholders, whereby Superior became a wholly owned subsidiary of DGSE Companies, Inc. Superior's principal line of business is the sale of rare coins on a retail, wholesale, and auction basis. Superior operates a store in Beverly Hills, CA. The total purchase price of approximately \$13.6 million was broken down as follows:

| | Shares | Stock Price | Extended Price |
|---------------------------|-----------|---------------------|----------------|
| Common stock | 3,669,067 | \$ 2.55 | \$ 9,356,121 |
| A warrants | 845,634 | 1.27 ⁽¹⁾ | 1,073,955 |
| B warrants | 863,000 | 2.55 | 2,200,650 |
| Exercise Price B warrants | 863,000 | \$.001 | (863) |
| Direct transaction costs | | | 1,176,290 |
| Total purchase price | | | \$ 13,806,153 |

(1)The \$1.27 is the fair value of the warrants calculated under the Black Sholes method as of the acquisition date.

The total purchase price has been allocated to the fair value of assets acquired and liabilities assumed as follows:

| | |
|---------------------------|--------------|
| Goodwill | \$ 8,203,448 |
| Intangible assets | 2,521,340 |
| Deferred tax asset | 1,860,475(1) |
| Property and other assets | 1,068,958 |

| | |
|----------------------|---------------|
| Inventory | 3,260,766 |
| Liabilities assumed | (3,108,834) |
| Total purchase price | \$ 13,806,153 |

- (1) Subsequent to date of acquisition the Company recorded an adjustment to reduce goodwill and increase deferred tax assets to reflect the change in estimated fair value of the net operating loss carryforwards acquired in the Superior acquisition.

DGSE COMPANIES, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements - *continued*
December 31, 2007, 2006 and 2005

In accordance with SFAS 142, the goodwill will not be amortized but instead tested for impairment in accordance with the provisions of SFAS 142 at least annually and more frequently upon the occurrence of certain events.

The operating results of Superior have been included in the consolidated financial statements since the acquisition date of May 30, 2007. The following unaudited pro forma condensed consolidated financial information reflects the results of operations for the year ended December 31, 2007 and 2006 as if the acquisition of Superior had occurred on January 1 of each year after giving effect to purchase accounting adjustments. These pro forma results have been prepared for comparative purposes only and do not purport to be indicative of what operating results would have been had the acquisition actually taken place at the beginning of the period, and may not be indicative of future operating results (in thousands, except per share data):

| <i>(In thousands, except per share data)</i> | Year Ended December 31, | |
|--|--------------------------------|-------------|
| | 2007 | 2006 |
| | (Unaudited) | |
| Pro forma total revenue | \$ 73,565 | \$ 83,487 |
| Pro forma net earnings (loss) | \$ (2,922) | \$ (3,135) |
| Pro forma net earnings per share — basic | \$ (.33) | \$ (0.50) |
| Pro forma net earnings per share — diluted | \$ (.33) | \$ (0.50) |
| Pro forma weighted average shares — basic | 8,582 | 6,226 |
| Pro forma weighted average shares — diluted | 10,353 | 6,320 |

In relation to the acquisition, as of June 29, 2007, Stanford and Dr. L.S. Smith, our chairman and chief executive officer, collectively had the power to vote approximately 63% of our voting securities, and beneficially owned approximately 56.4% of our voting securities on a fully-diluted basis (after giving effect to the exercise of all options and warrants held by them which are exercisable within sixty days of June 29, 2007 but not giving effect to the exercise of any other options or warrants). Consequently, these two stockholders may have sufficient voting power to control the outcome of virtually all corporate matters submitted to the vote of our common stockholders. Those matters could include the election of directors, changes in the size and composition of our board of directors, mergers and other business combinations involving us, or the liquidation of our company. In addition, Stanford and Dr. Smith have entered into a corporate governance agreement with us, which entitles Stanford and Dr. Smith to each nominate two “independent” directors to our board and entitles Dr. Smith, our chairman and chief executive officer, and William H. Oyster, our president and chief operating officer, to be nominated to our board for so long as each remains an executive officer.

Through this control of company nominations to our board of directors and through their voting power, Stanford and Dr. Smith are able to exercise substantial control over certain decisions, including decisions regarding the qualification and appointment of officers, dividend policy, access to capital (including borrowing from third-party lenders and the issuance of additional equity securities), a merger or consolidation with another company, and our acquisition or disposition of assets. Also, the concentration of voting power in the hands of Stanford and Dr. Smith could have the effect of delaying or preventing a change in control of our company, even if the change in control would benefit our other stockholders. The significant concentration of stock ownership may adversely affect the trading price of our common stock due to investors’ perception that conflicts of interest may exist or arise.

Eulless Gold & Silver, Inc.

On May 9, 2007 we purchased all of the tangible assets of Euless Gold and Silver, Inc., located in Euless, Texas. The purchase price paid for these assets totaled \$1,000,000 including \$600,000 in cash and a two year note in the amount of \$400,000. We opened a new retail store in the former Euless Gold & Silver facility and operate under the name of Dallas Gold & Silver Exchange. Of the assets received, \$990,150 was inventory and the remainder was fixed assets.

DGSE COMPANIES, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements - *continued*
December 31, 2007, 2006 and 2005

We entered into these transactions seeing them as opportunistic acquisitions that would allow us to expand our operations and provide a platform for future growth.

Note 7 - Goodwill

The Company recognized an increase in goodwill as a result of the Superior Galleries, Inc. acquisition during 2007. At December 31, goodwill was reflected for the following reporting units:

| | 2007 | 2006 |
|--------------------------|--------------|------------|
| Superior Galleries, Inc. | \$ 8,115,064 | — |
| Wholesale watch sales | \$ 837,117 | \$ 837,117 |
| Total Goodwill | \$ 8,952,181 | \$ 837,117 |

No impairment losses were recognized during 2007, 2006 or 2005.

Note 8 - Auction and Customer Advances

Superior has established two short-term lending programs consisting of (i) advancing consignment customers cash based on consigned inventory acquired for upcoming auctions, and, (ii) advancing customers cash based on the customer's assigning specific rare coins in their inventory to Superior as collateral. According to the terms of its Commercial Line of Credit, Superior can advance a customer up to 70% of consigned or assigned rare coin(s), wholesale value. For auction advances, Superior will advance cash to the customer and take control of the inventory to be held on consignment for auction. The customer will sign a note receivable for the funds advanced to be secured by the consigned inventory. As consigned inventory is sold, the proceeds will be collected, repaying Superior for the auction advance and any auction fees, with the remaining amount due to the consignor. For customer inventory advances, Superior will advance cash to a customer and take control of the assigned inventory. The customer will sign a promissory note for the funds advanced to be secured by the assigned inventory. Auction and customer advances bear interest at rates between 10% and 18% based primarily on the customer's creditworthiness and the loan size. The average term of the loan is approximately three months and no individual loan will exceed one year. Customers may require minimum prices for their consigned coins, and if the coin has not sold by the loan maturity date, the customer must choose to refinance the loan, repay the loan, or permit Superior to liquidate the coin. Superior will retain control of the assigned inventory until the customer repays the advance. Auction and customer advances consist of the follows:

| | December 31, 2007 | December 31, 2006 |
|------------------|----------------------|----------------------|
| Auction advances | \$ 747,000 | \$ — |
| | \$ 747,000 | \$ — |

Note 9 - Notes Payable

At December 31, 2007, the Company was obligated to various individuals under unsecured, demand notes bearing annual interest rates of 8% to 12% totaling \$187,468.

At December 31, 2006, the Company was obligated to various individuals under unsecured, demand notes bearing annual interest rates of 8% to 12% totaling \$183,708.

At December 31, 2005, the Company was obligated to various individuals under unsecured, demand notes bearing annual interest rates of 8% to 12% totaling \$594,183.

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DGSE COMPANIES, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements - *continued*
December 31, 2007, 2006 and 2005

Note 10 - Long-Term Debt

| | 2007 | 2006 |
|--|---------------|--------------|
| A summary of long-term debt at December 31, follows: | | |
| Revolving promissory notes payable to bank, a note of \$3,595,000 and \$2,985,000 at December 31, 2007 and 2006, respectively, which bears interest at prime plus 1-1/2% (9.50% and 9.75% at December 31, 2007 and 2006, respectively, and is due June 22, 2009 and a note of \$1,000,000 which bears interest at prime plus 1-3/4% (10.0% and 9.0% at December 31, 2006 and 2005), respectively, is due in equal monthly installments of \$16,667 through June 2009. Balance of note was \$584,721 and \$800,000 as of December 31, 2007 and 2006, respectively. The defined borrowing base requirement is based on eligible trade receivables and inventory. As of December 31, 2007, available but unused borrowing capacity on the revolver was \$0. These notes are secured by all accounts receivable, inventory, property and equipment and intangible assets. The notes contain certain covenants, restricting payment of dividends, and requiring the Company to maintain certain financial ratios. In addition to the above, the Company has an additional \$11,500,000 line of credit with Stanford International Bank, LTD. Interest on this facility is at the prime rate, as reported in the Wall Street Journal and the facility will mature and become due in May 2011. Of this line, \$6,700,000 has been drawn against, most of which related to the Superior Galleries acquisition. As of December 31, 2007, \$4,800,000 was available to us. | \$ 10,879,721 | \$ 3,785,000 |
| Our current mortgage payable as of December 31, 2007 is due in monthly installments of \$22,744, including interest of 6.70% with a balance due in August 2016. Our old mortgage payable reflected for 2006 was due in monthly installments of \$5,881, including interest based on 30 year U.S. Treasury note rate plus 2-1/2% (7.23% at December 31, 2006) with a then balance due in January 2014 | 2,435,364 | 386,770 |
| Note payable, due in quarterly payments of \$57,691 including interest of 8.25%. The final payment is due May 1, 2009 | 315,128 | — |
| Note payable, due January 2, 2009. Interest is payable monthly at a rate of 8% | 310,556 | 310,556 |
| Capital lease obligations | 50,763 | 80,632 |
| | 13,991,532 | 4,562,958 |
| Less current maturities | (501,631) | (259,273) |
| | \$ 13,489,901 | \$ 4,303,685 |

The following table summarizes the aggregate maturities of long-term debt and payments on the capital lease obligations and reflects the revised maturities from refinancing of certain long-term debt subsequent to year-end:

| December 31, | Long-term Debt | Obligations under Capital Leases | Totals |
|----------------------|----------------|-------------------------------------|---------------|
| 2008 | \$ 485,948 | \$ 15,683 | 501,631 |
| 2009 | 4,177,763 | 21,048 | 4,198,811 |
| 2010 | 93,278 | 14,032 | 107,310 |
| 2011 | 6,799,723 | — | 6,799,723 |
| 2012 | 106,614 | — | 106,614 |
| Thereafter | 2,277,443 | — | 2,277,443 |
| | 13,940,769 | 50,763 | 13,991,532 |
| Less current portion | (485,948) | (15,683) | (501,631) |
| | \$ 13,454,821 | \$ 35,080 | \$ 13,489,901 |

DGSE COMPANIES, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements - *continued*
December 31, 2007, 2006 and 2005

Note 11 - Earnings Per Common Share

A reconciliation of the income and shares of the basic earnings per common share and diluted earnings per common share for the years ended December 31, 2007, 2006 and 2005 is as follows:

| Net Earnings | Shares | | Per Share |
|-------------------------------------|---------------------------------------|-----------|-----------|
| | (In thousands, except per share data) | | |
| Year ended December 31, 2007 | | | |
| Basic earnings per common share | \$ 755,019 | 7,507,579 | \$ 0.10 |
| Effect of dilutive stock options | — | 774,308 | |
| Diluted earnings per common share | \$ 755,019 | 8,281,887 | \$ 0.09 |
| Year ended December 31, 2006 | | | |
| Basic earnings per common share | \$ 611,245 | 4,913,920 | \$ 0.12 |
| Effect of dilutive stock options | — | 92,989 | |
| Diluted earnings per common share | \$ 611,245 | 5,006,909 | \$ 0.12 |
| Year ended December 31, 2005 | | | |
| Basic earnings per common share | \$ 485,192 | 4,913,920 | \$ 0.10 |
| Effect of dilutive stock options | (4,554) | 123,783 | |
| Diluted earnings per common share | \$ 485,192 | 5,037,073 | \$ 0.10 |

Note 12 - Stock Options

The Company has granted stock options to key employees and directors to purchase shares of the Company's common stock. Each option issued vests according to schedules designated by the Board of Directors, not to exceed three years. The exercise price is based upon the estimated fair market value of the Company's common stock at the date of grant, and is payable when the option is exercised.

Prior to January 1, 2006, the Company elected to follow Accounting Principles Board Opinion (APB) NO.25, *Accounting for Stock Issued to Employees*, and related interpretations to account for its employee and director stock options, as permitted by Statement of Financial Accounting Standards (SFAS) No. 123, *Accounting for Stock-Based Compensation*. Effective January 1, 2006, the Company adopted the fair value recognition provision of SFAS No. 123 (revised 2004), *Share-Based Payments*, (SFAS No. 123(R) for all share-based payment awards to employees and directors including employee stock options. In addition, the Company has applied the provisions of Staff Accounting Bulletin No. 107 (SAB No. 107), issued by the Securities and Exchange Commission, in our adoption of SFAS No. 123(R).

The Company adopted SFAS No. 123(R) using the modified-prospective-transition method. Under this transition method, stock-based compensation expense recognized after the effective date includes: (1) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimate in accordance with the original provisions of SFAS No. 123, and (2) compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant-date fair value estimate in accordance with the provision of SFAS No. 123. Results from prior periods have not been restated and do not include the impact of SFAS No. 123(R). Stock-based compensation expense under SFAS No. 123(R) for the year ended December 31, 2007 and 2006 was \$28,817 and \$0, respectively, relating to employee and director stock options and our employee stock purchase plan. Stock-based compensation expense under the provision of APB No. 25 for the year ended December 31, 2006 was insignificant.

DGSE COMPANIES, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements - *continued*
December 31, 2007, 2006 and 2005

Stock-based compensation expense recognized each period is based on the value of the portion of share-based payment awards that is ultimately expected to vest during the period. SFAS No. 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. In our pro forma disclosures required under SFAS No. 123 for periods prior to 2006, the Company accounted for forfeitures as they occurred.

Upon adoption of SFAS No. 123(R), the Company elected to use the Black-Scholes-Merton option-pricing formula to value share-based payments granted to employees subsequent to January 1, 2006 and elected to attribute the value of stock-based compensation to expense using the straight-line single option method. These methods were previously used for the Company's pro forma information required under SFAS No. 123.

On November 10, 2005, the Financial Accounting Standards Board (FASB) issued FASB Staff Position No. FAS 123(R)-3, "Transition Election Related to Accounting for Tax Effects of Share-Based Payment Awards", which detailed an alternative transition method for calculating the tax effects of stock-based compensation pursuant to SFAS No. 123(R). This alternative transition method included simplified methods to establish the beginning balance of the additional paid-in capital pool (APIC pool) related to the tax effects of employee stock-based compensation and to determine the subsequent impact on the APIC pool and Consolidated Statement of Cash Flows of the tax effects of employee stock-based compensation awards that are outstanding upon adoption of SFAS No. 123(R). As of December 31, 2007, we have not recorded the tax effects of employee stock-based compensation and have made no adjustments to the APIC pool.

SFAS No. 123(R) requires the cash flows resulting from the tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows. As there have been no stock options exercised, we have not reported these excess tax benefits as of December 31, 2007.

The following table summarizes the activity in common shares subject to options for the years ended December 31, 2007, 2006 and 2005:

| | 2007 | | At December 31, 2006 | | 2005 | |
|------------------------------------|-----------|--|-------------------------|--|-----------|--|
| | Shares | Weighted average exercise price | Shares | Weighted average exercise price | Shares | Weighted average exercise price |
| Outstanding at beginning of year | 1,403,134 | \$ 2.03 | 1,403,134 | \$ 2.03 | 1,420,634 | \$ 2.09 |
| Granted | 50,000 | 6.00 | — | 0.00 | 35,000 | 2.60 |
| Exercised | — | 0.00 | — | 0.00 | — | 0.00 |
| Forfeited | (10,000) | 0.00 | — | 0.00 | (52,500) | 4.10 |
| Outstanding at end of year | 1,443,134 | \$ 2.17 | 1,403,134 | \$ 2.03 | 1,403,134 | \$ 2.03 |
| Options exercisable at end of year | 1,393,134 | \$ 2.17 | 1,403,134 | \$ 2.03 | 1,403,134 | \$ 2.03 |

During the year ended December 31, 2007, there have been 50,000 options granted to our non-employee directors under this plan and, as a result, there are 700,000 shares available for future grants under the 2006 Plan.

DGSE COMPANIES, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements - continued
December 31, 2007, 2006 and 2005

Information about Plan stock options outstanding at December 31, 2007 is summarized as follows:

| Range of exercise prices | Number outstanding | Options outstanding | |
|--------------------------|-----------------------|--|---------------------------------------|
| | | Weighted average remaining contractual life | Weighted average exercise price |
| \$1.12 | 267,857 | 5 years | \$ 1.12 |
| \$1.13 to \$2.25 | 1,072,777 | 5 years | \$ 2.21 |
| \$2.26 to \$2.82 | 35,000 | 5 years | \$ 2.60 |
| \$2.83 to \$4.19 | 17,500 | 2 years | \$ 3.88 |
| \$6.00 | 50,000 | 10 years | \$ 6.00 |
| | 1,443,134 | | |

| Range of exercise prices | Options exercisable | |
|--------------------------|-----------------------|---------------------------------------|
| | Number exercisable | Weighted average exercise price |
| \$1.12 | 267,857 | \$ 1.12 |
| \$1.13 to \$2.25 | 1,072,777 | \$ 2.21 |
| \$2.26 to \$2.82 | 35,000 | \$ 2.60 |
| \$2.83 to \$4.19 | 17,500 | \$ 3.88 |
| | 1,393,134 | |

Note 13 - Comprehensive Income

Comprehensive income at December 31, 2007, 2006 and 2005 is as follows:

| | Before-Tax Amount | Tax Benefit | Net-of-Tax Amount |
|--|----------------------|-------------|----------------------|
| Accumulated comprehensive income (loss) at January 1, 2005 | \$ (150,784) | \$ 28,202 | \$ (122,582) |
| Unrealized holding losses arising during 2005 | (11,287) | 6,617 | (4,994) |
| Accumulated comprehensive income (loss) at December 31, 2005 | (162,071) | 34,819 | (127,252) |
| Unrealized holding losses arising during 2006 | (7,519) | 2,526 | (4,993) |
| Accumulated comprehensive income (loss) at December 31, 2006 | (169,590) | 37,345 | (132,245) |
| Unrealized holding gains arising during 2007 | 25,714 | 9,243 | 34,957 |
| Accumulated comprehensive income (loss) at December 31, 2007 | (143,876) | 46,588 | (97,288) |

Note 14 - Intangible Assets

Intangible assets represent the customer base and trade name resulting from the Superior Acquisition as follows:

| | December 31, 2007 | December 31, 2006 |
|-------------------|-------------------|-------------------|
| Customer base | \$ 430,000 | \$ — |
| Trade name | \$ 2,091,340 | — |
| Intangible assets | \$ 2,521,340 | \$ — |

Only the customer base intangible asset will be subject to amortization and will be amortized over a 15 year life. The monthly amortization of \$28,667 will begin in the first quarter of 2008 upon final assessment and adjustments are recorded to the purchase price.

DGSE COMPANIES, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements - *continued*
December 31, 2007, 2006 and 2005

Note 15 - Income Taxes

The income tax provision reconciled to the tax computed at the statutory Federal rate follows:

| | 2007 | 2006 | 2005 |
|------------------------------------|----------|---------|------------|
| Tax expense at statutory rate | 272,658 | 316,484 | \$ 256,609 |
| Other | 8,576 | 3,323 | 12,933 |
| Benefit of discontinued operations | (38,830) | — | — |
| Tax expense | 242,404 | 319,807 | \$ 269,542 |
| Current | 77,424 | 323,653 | \$ 247,710 |
| Deferred | 164,980 | (3,846) | 21,832 |
| Total | 242,404 | 319,807 | \$ 269,542 |

Deferred income taxes are comprised of the following at December 31, 2007 and 2006:

| | 2007 | 2006 |
|--|--------------|-----------|
| Deferred tax assets (liabilities): | | |
| Inventory | 90,546 | \$ 62,077 |
| Unrealized loss on available for sale securities | 46,588 | 37,345 |
| Property and equipment | (12,764) | (78,446) |
| Capital loss carryover | 8,366 | 16,457 |
| Superior acquisition | 1,766,361 | — |
| Goodwill | (93,892) | (95,715) |
| Total deferred tax assets | \$ 1,805,205 | \$ 7,152 |

Note 16 - Operating Leases

The Company leases certain of its facilities under operating leases. The minimum rental commitments under noncancellable operating leases as of December 31, 2007 are as follows:

| Year Ending December 31, | Lease Obligations |
|-----------------------------|----------------------|
| 2008 | \$ 771,529 |
| 2009 | 822,574 |
| 2010 | 695,903 |
| 2011 | 658,392 |
| Thereafter | 540,092 |
| | \$ 3,488,490 |

Rent expense for the years ended December 31, 2007, 2006 and 2005 was approximately \$437,069, \$201,810 and \$174,988, respectively, was decreased by sublease income of approximately \$0, \$0 and \$45,300, respectively.

Note 17 - Discontinued Operations

On July 13, 2007, we sold the loan balances from our American Pay Day Center locations for \$77,496 and discontinued operations in those locations. The receivables sold, including interest due, had a balance of \$120,573 at

the time of the sale. The sales price was determined based on the age of the outstanding receivables. As a result of the sale and discontinued operations, we recognized a pretax loss of \$107,838 on the disposal and a pretax loss on discontinued operations of \$51,938 for the year ended December 31, 2007. As a result, operating results from this subsidiary have been reclassified to discontinued operations for all periods presented. As of December 31, 2007 there were no operating assets to be disposed of or liabilities to be paid in completing the disposition of these operations.

DGSE COMPANIES, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements - continued
December 31, 2007, 2006 and 2005

Note 18 - Segment Information

Management identifies reportable segments by product or service offered. Each segment is managed separately. Corporate and other includes certain general and administrative expenses not allocated to segments, pay day lending and pawn operations. The Company's operations by segment were as follows:

| <i>(In thousands)</i> | Retail Jewelry | Wholesale Jewelry | Bullion | Rare Coins | Auctions | Corporate and Other | Consolidated |
|--------------------------------------|---------------------------|------------------------------|----------------|-----------------------|-----------------|------------------------------------|---------------------|
| Revenues | | | | | | | |
| 2007 | \$ 19,338 | \$ 5,785 | \$ 21,153 | \$ 13,921 | \$ 1,498 | \$ 1,271 | \$ 62,966 |
| 2006 | 16,519 | 5,997 | 16,252 | 4,697 | — | 618 | 44,083 |
| 2005 | 14,917 | 4,781 | 10,688 | 4,575 | — | 679 | 35,640 |
| Net income (loss) | | | | | | | |
| 2007 | 319 | 197 | 235 | 8 | 42 | (46) | 755 |
| 2006 | 143 | 270 | 148 | 101 | — | (51) | 611 |
| 2005 | 195 | 250 | 79 | 267 | — | (306) | 485 |
| Identifiable assets | | | | | | | |
| 2007 | 16,132 | 2,164 | 536 | 4,314 | 2,139 | 11,574 | 36,859 |
| 2006 | 10,020 | 1,940 | 114 | 235 | — | 837 | 13,146 |
| 2005 | 9,015 | 1,733 | 209 | 203 | — | 670 | 11,830 |
| Capital Expenditures | | | | | | | |
| 2007 | 3,126 | — | 23 | — | — | 274 | 3,423 |
| 2006 | 11 | — | — | — | — | 31 | 42 |
| 2005 | 202 | — | — | — | — | 83 | 285 |
| Depreciation and amortization | | | | | | | |
| 2007 | 130 | — | 33 | 32 | 32 | 27 | 254 |
| 2006 | 107 | — | — | — | — | 32 | 139 |
| 2005 | 107 | 10 | — | — | — | 25 | 142 |

Note 19 - Quarterly Results of Operations (Unaudited)

| | 1st Quarter | 2nd Quarter | 3rd Quarter | 4th Quarter |
|-------------------------------------|--|--------------------|--------------------|--------------------|
| | (In thousands, except per share data) | | | |
| Year ended December 31, 2007 | | | | |
| Revenues | \$ 10,240 | \$ 12,577 | \$ 16,856 | \$ 23,294 |
| Operating profit | 384 | 557 | 142 | 174 |
| Net earnings | 182 | 278 | 284 | 11 |
| Basic earnings per common share | \$ 0.04 | \$ 0.05 | \$ 0.03 | \$ 0.00 |
| Diluted earnings per common share | \$ 0.04 | \$ 0.04 | \$ 0.03 | \$ 0.00 |
| Year ended December 31, 2006 | | | | |
| Revenues | \$ 9,721 | \$ 12,546 | \$ 9,609 | \$ 12,207 |

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| | | | | | | | | |
|-------------------------------------|----|-------|----|-------|----|-------|----|--------|
| Operating profit | | 302 | | 484 | | 242 | | 295 |
| Net earnings | | 148 | | 271 | | 108 | | 84 |
| Basic earnings per common share | \$ | 0.03 | \$ | 0.05 | \$ | 0.02 | \$ | 0.02 |
| Diluted earnings per common share | \$ | 0.03 | \$ | 0.05 | \$ | 0.02 | \$ | 0.02 |
| Year ended December 31, 2005 | | | | | | | | |
| Revenues | \$ | 6,718 | \$ | 6,800 | \$ | 7,215 | \$ | 14,906 |
| Operating profit | | 299 | | 192 | | 206 | | 330 |
| Net earnings | | 151 | | 79 | | 92 | | 164 |
| Basic earnings per common share | \$ | 0.03 | \$ | 0.02 | \$ | 0.02 | \$ | 0.03 |
| Diluted earnings per common share | \$ | 0.03 | \$ | 0.02 | \$ | 0.02 | \$ | 0.03 |

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