

EVOLUTION PETROLEUM CORP

Form 10-Q

February 08, 2019

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended December 31, 2018

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 001-32942

EVOLUTION PETROLEUM CORPORATION

(Exact name of registrant as specified in its charter)

Nevada

(State or other jurisdiction of incorporation or organization)

41-1781991

(IRS Employer Identification No.)

1155 Dairy Ashford Road, Suite 425, Houston, Texas 77079

(Address of principal executive offices and zip code)

(713) 935-0122

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes:  No:

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

Emerging growth company

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

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

The number of shares outstanding of the registrant's common stock, par value \$0.001, as of February 4, 2019, was 33,186,665.

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EVOLUTION PETROLEUM CORPORATION AND SUBSIDIARIES

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## PART I — FINANCIAL INFORMATION

## ITEM 1. CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

Evolution Petroleum Corporation and Subsidiaries  
Consolidated Condensed Balance Sheets  
(Unaudited)

	December 31, 2018	June 30, 2018
Assets		
Current assets		
Cash and cash equivalents	\$ 30,000,801	\$24,929,844
Restricted cash	—	2,751,289
Receivables	3,434,227	3,941,916
Prepaid expenses and other current assets	594,555	524,507
Total current assets	34,029,583	32,147,556
Oil and natural gas property and equipment, net (full-cost method of accounting)	62,137,689	61,239,746
Other property and equipment, net	24,187	30,407
Total property and equipment	62,161,876	61,270,153
Other assets	228,405	244,835
Total assets	\$ 96,419,864	\$93,662,544
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	\$ 2,705,359	\$3,432,568
Accrued liabilities and other	363,208	874,886
State and federal income taxes payable	136,124	122,760
Total current liabilities	3,204,691	4,430,214
Long term liabilities		
Senior secured credit facility (Note 13)	—	—
Deferred income taxes	11,061,732	10,555,435
Asset retirement obligations	1,467,646	1,387,416
Total liabilities	15,734,069	16,373,065
Commitments and contingencies (Note 14)		
Stockholders' equity		
Common stock; par value \$0.001; 100,000,000 shares authorized; 33,186,665 and 33,080,543 shares issued and outstanding as of December 31, 2018 and June 30, 2018, respectively	33,186	33,080
Additional paid-in capital	42,088,385	41,757,645
Retained earnings	38,564,224	35,498,754
Total stockholders' equity	80,685,795	77,289,479
Total liabilities and stockholders' equity	\$ 96,419,864	\$93,662,544

See accompanying notes to consolidated condensed financial statements.

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Consolidated Condensed Statements of Operations  
(Unaudited)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2018	2017	2018	2017
Revenues				
Crude oil	\$10,515,875	\$10,185,635	\$21,913,327	\$18,014,890
Natural gas liquids	532,243	740,585	1,441,870	1,313,297
Total revenues	11,048,118	10,926,220	23,355,197	19,328,187
Operating costs				
Production costs	3,452,168	2,773,821	6,910,598	5,529,503
Depreciation, depletion and amortization	1,603,633	1,656,891	3,152,093	3,197,013
General and administrative expenses *	1,258,570	1,666,256	2,563,832	3,235,960
Total operating costs	6,314,371	6,096,968	12,626,523	11,962,476
Income from operations	4,733,747	4,829,252	10,728,674	7,365,711
Other				
Enduro transaction breakup fee	—	—	1,100,000	—
Interest and other income	59,858	15,841	106,429	30,691
Interest expense	(29,345)	(20,456)	(58,690)	(40,911)
Income before income taxes	4,764,260	4,824,637	11,876,413	7,355,491
Income tax provision (benefit)	859,695	(5,052,211)	2,176,047	(4,661,889)
Net income available to common stockholders	\$3,904,565	\$9,876,848	\$9,700,366	\$12,017,380
Earnings per common share				
Basic	\$0.12	\$0.30	\$0.29	\$0.36
Diluted	\$0.12	\$0.30	\$0.29	\$0.36
Weighted average number of common shares				
Basic	33,167,159	33,109,448	33,134,726	33,099,546
Diluted	33,176,503	33,140,278	33,147,775	33,140,257

\* General and administrative expenses for the three months ended December 31, 2018 and 2017 included non-cash stock-based compensation of \$254,111 and \$484,326, respectively. For the six months ended December 31, 2018 and 2017, non-cash stock-based compensation expenses were \$469,484 and \$971,810 respectively.

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Consolidated Condensed Statements of Cash Flows  
(Unaudited)

	Six Months Ended December 31,	
	2018	2017
Cash flows from operating activities		
Net income attributable to the Company	\$9,700,366	\$12,017,380
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion and amortization	3,159,671	3,225,147
Stock-based compensation	469,484	971,810
Deferred income tax expense (benefit)	506,297	(5,245,910 )
Changes in operating assets and liabilities:		
Receivables	507,689	(1,351,451 )
Prepaid expenses and other current assets	(70,048 )	(436,376 )
Accounts payable and accrued expenses	(142,568 )	(83,013 )
Income taxes payable	13,364	—
Net cash provided by operating activities	14,144,255	9,097,587
Cash flows from investing activities		
Capital expenditures for oil and natural gas properties	(5,048,987 )	(1,017,358 )
Capital expenditures for other property and equipment	(2,066 )	—
Net cash used in investing activities	(5,051,053 )	(1,017,358 )
Cash flows from financing activities		
Cash dividends to common stockholders	(6,634,896 )	(4,969,335 )
Common share repurchases, including shares surrendered for tax withholding	(138,638 )	(395,550 )
Net cash used in financing activities	(6,773,534 )	(5,364,885 )
Net increase in cash, cash equivalents and restricted cash	2,319,668	2,715,344
Cash, cash equivalents and restricted cash, beginning of period	27,681,133	23,028,153
Cash, cash equivalents and restricted cash, end of period	\$30,000,801	\$25,743,497
Supplemental disclosures of cash flow information:		Six Months Ended December 31,
		2018      2017
Income taxes paid		\$1,862,919   \$1,136,754
Non-cash transactions:		
Change in accounts payable used to acquire property and equipment		(1,094,249 ) 424,365
Oil and natural gas property costs incurred through recognition of asset retirement obligations		31,268      (779 )

See accompanying notes to consolidated condensed financial statements.

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Evolution Petroleum Corporation and Subsidiaries  
 Consolidated Condensed Statement of Changes in Stockholders' Equity  
 For the Six Months Ended December 31, 2018  
 (Unaudited)

	Common Stock		Additional	Retained	Treasury	Total
	Shares	Par Value	Paid-in Capital	Earnings	Stock	Stockholders' Equity
Balance at June 30, 2018	33,080,543	\$33,080	\$41,757,645	\$35,498,754	\$ —	\$77,289,479
Issuance of restricted common stock	121,611	122	(122 )	—	—	—
Common share repurchases, including shares surrendered for tax withholding	(15,489 )	—	—	—	(138,638)	(138,638 )
Retirements of treasury stock	—	(16 )	(138,622 )	—	138,638	—
Stock-based compensation	—	—	469,484	—	—	469,484
Net income attributable to the Company	—	—	—	9,700,366	—	9,700,366
Common stock cash dividends, \$0.10 per share	—	—	—	(6,634,896 )	—	(6,634,896 )
Balance at December 31, 2018	33,186,665	\$33,186	\$42,088,385	\$38,564,224	\$ —	\$80,685,795

See accompanying notes to consolidated condensed financial statements.



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Evolution Petroleum Corporation And Subsidiaries

Notes to Unaudited Consolidated Condensed Financial Statements

Note 1 — Organization and Basis of Preparation

**Nature of Operations.** Evolution Petroleum Corporation ("EPM") is an oil and gas company focused on delivering a sustainable dividend yield to its stockholders through the ownership, management and development of producing oil and gas properties. The Company's long-term goal is to build a diversified portfolio of oil and gas assets primarily through acquisition, while seeking opportunities to maintain and increase production through selective development, production enhancement and other exploitation efforts on its properties. Our largest active investment is our interest in a CO<sub>2</sub> enhanced oil recovery project in Louisiana's Delhi field.

**Interim Financial Statements.** The accompanying unaudited consolidated condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and the appropriate rules and regulations of the Securities and Exchange Commission ("SEC"). Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to such rules and regulations. All adjustments (consisting of normal recurring accruals) which are, in the opinion of management, necessary for a fair presentation of the financial position and results of operations for the interim periods presented have been included. The interim financial information and notes hereto should be read in conjunction with the Company's 2018 Annual Report on Form 10-K for the fiscal year ended June 30, 2018, as filed with the SEC. The results of operations for interim periods are not necessarily indicative of results to be expected for a full fiscal year.

**Principles of Consolidation and Reporting.** Our consolidated financial statements include the accounts of EPM and its wholly-owned subsidiaries (the "Company"). All significant intercompany transactions have been eliminated in consolidation. The consolidated financial statements for the previous year may include certain reclassifications to conform to the current presentation. Any such reclassifications have no impact on previously reported net income or stockholders' equity.

**Use of Estimates.** The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Significant estimates include (a) reserve quantities and estimated future cash flows associated with proved reserves, which significantly impact depletion expense and potential impairments of oil and natural gas properties, (b) asset retirement obligations, (c) stock-based compensation, (d) fair values of derivative assets and liabilities, (e) income taxes and the valuation of deferred tax assets and (f) commitments and contingencies. We analyze our estimates based on historical experience and various other assumptions that we believe to be reasonable. While we believe that our estimates and assumptions used in preparation of the consolidated financial statements are appropriate, actual results could differ from those estimates.

Note 2 — Summary of Significant Accounting Policies

Revenue Recognition

Effective July 1, 2018, the Company adopted ASU No. 2014-09, Revenue From Contracts With Customers (Topic 606) ("ASC 606") using the full retrospective method and has applied the standard to all existing contracts. ASC 606 supersedes previous revenue recognition requirements in ASC 605 - Revenue Recognition ("ASC 605") and includes a five-step revenue recognition model to depict the transfer of goods or services to customers in an amount that reflects the consideration in exchange for those goods or services. As a result of adopting ASC 606, the Company did not have a cumulative-effect adjustment in retained earnings. The comparative information presented therein for the three and six months ended December 31, 2017 reflects the reclassification on our consolidated statement of operations of

\$140,691 and \$276,595, respectively, from “Production Costs” to “Revenue - Natural Gas Liquids” in conformance with ASC 606. These changes to revenue and production costs resulted from the conclusion that the Company did not control the product throughout processing before transferring to the customer. Therefore, costs incurred after the transfer of control are treated as reductions of revenue. Additionally, adoption of ASC 606 did not impact net income attributable to common stockholders, current assets, total assets, current liabilities, total liabilities or stockholders’ equity and the Company does not expect that it will do so in future periods.

Our revenues are comprised solely of revenues from customers from the sale of crude oil and NGLs. The Company believes that the disaggregation of revenue on its consolidated statements of operations into these two major product types appropriately depicts how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors based on our single geographic location. Crude oil and NGL revenues are recognized at a point in time when production is sold to a purchaser at an index-based, determinable price, delivery has occurred, control has transferred and collectibility of

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Evolution Petroleum Corporation And Subsidiaries

Notes to Unaudited Consolidated Condensed Financial Statements

the revenue is probable. The transaction price used to recognize revenue is a function of the contract billing terms which reference index price sources used by the industry. Revenue is invoiced by calendar month based on volumes at contractually based rates with payment typically required within 30 days for crude oil and 60 days for NGLs after the end of the production month. At the end of each month when the performance obligations have been satisfied, the consideration can be reasonably estimated and amounts due from customers are accrued in "Receivables" in our consolidated balance sheets. As of December 31, 2018 and June 30, 2018, receivables from contracts with customers were \$3.4 million and \$3.9 million, respectively.

**Other Recently Adopted Accounting Pronouncements**

In January 2016, the FASB issued ASU 2016-01, Financial Instruments - Overall: Recognition and Measurement of Financial Assets and Financial Liabilities ("ASU 2016-01"). The pronouncement requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investees) to be measured at fair value with changes in fair value recognized in net income, requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset, and eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. Effective July 1, 2018, the Company prospectively adopted ASU 2016-01 without impact to its consolidated financial position or results of operations. Because its investment in Well Lift Inc. does not have a readily determinable fair value, the Company elected to measure this investment at cost less impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer, if they were to occur.

Effective July 1, 2018, the Company retrospectively adopted ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, which is intended to reduce diversity in practice in how certain transactions are classified in the statement of cash flows. The guidance addresses eight specific cash flow issues for which current GAAP is either unclear or does not include specific guidance. Adoption had no effect on our current period and comparative consolidated statements of cash flows.

Effective July 1, 2018, the Company prospectively adopted ASU No. 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business, which clarifies the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The Company will apply the clarified definition of business to future acquisitions and divestitures.

**Recently Issued Accounting Pronouncements**

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) ("ASU 2016-02"), which relates to the accounting for leasing transactions. This standard requires a lessee to record on the balance sheet the assets and liabilities for the rights and obligations created by leases with lease terms of more than twelve months. In addition, this standard requires both lessees and lessors to disclose certain key information about lease transactions. This standard will be effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. We are evaluating the impact the adoption of ASU 2016-02 will have on our consolidated financial statements.

**Note 3 — Receivables**

As of December 31, 2018 and June 30, 2018, our receivables consisted of the following:

	December 31, 2018	June 30, 2018
Receivables from oil and NGL sales	\$ 3,434,227	\$3,940,998
Other	—	918
Total receivables	\$ 3,434,227	\$3,941,916



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Notes to Unaudited Consolidated Condensed Financial Statements

## Note 4 — Prepaid Expenses and Other Current Assets

As of December 31, 2018 and June 30, 2018, our prepaid expenses and other current assets consisted of the following:

	December 31, June 30,	
	2018	2018
Prepaid insurance	\$ 87,234	\$198,558
Retainers and deposits	6,089	11,089
Prepaid federal and state income taxes	438,453	231,920
Other prepaid expenses	62,779	82,940
Prepaid expenses and other current assets	\$ 594,555	\$524,507

## Note 5 — Property and Equipment

As of December 31, 2018 and June 30, 2018, our oil and natural gas properties and other property and equipment consisted of the following:

	December 31, June 30,	
	2018	2018
Oil and natural gas properties		
Property costs subject to amortization	\$94,378,924	\$90,392,918
Less: Accumulated depreciation, depletion, and amortization	(32,241,235 )	(29,153,172 )
Unproved properties not subject to amortization	—	—
Oil and natural gas properties, net	\$62,137,689	\$61,239,746
Other property and equipment		
Furniture, fixtures, office equipment and other, at cost	\$145,289	\$143,223
Less: Accumulated depreciation	(121,102 )	(112,816 )
Other property and equipment, net	\$24,187	\$30,407

During the six months ended December 31, 2018 and 2017, the Company incurred capital expenditures of \$4.0 million and \$1.4 million, respectively, in the Delhi field.

## Note 6 — Other Assets

As of December 31, 2018 and June 30, 2018, other assets consisted of the following:

	December 31, June 30,	
	2018	2018
Royalty rights	\$ 108,512	\$108,512
Less: Accumulated amortization of royalty rights	(40,692 )	(33,910 )
Investment in Well Lift Inc., at cost	108,750	108,750
Deferred loan costs	168,972	168,972
Less: Accumulated amortization of deferred loan costs	(134,349 )	(126,771 )
Software license	20,662	20,662
Less: Accumulated amortization of software license	(3,450 )	(1,380 )
Other assets, net	\$ 228,405	\$244,835

Our royalty rights and investment in Well Lift, Inc. ("WLI") resulted from the separation of our artificial lift technology operations in December 2015. We conveyed our patents and other intellectual property to WLI and retained a 5% royalty on future gross revenues associated the technology. We own 17.5% of the common stock of

WLI and account for our investment in this private company at cost less impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer, if such were to occur. The Company evaluates the investment for impairment when it identifies any events or changes in circumstances that might have a significant adverse effect on the fair value of the investment.

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Notes to Unaudited Consolidated Condensed Financial Statements

## Note 7 — Accrued Liabilities and Other

As of December 31, 2018 and June 30, 2018, our other current liabilities consisted of the following:

	December 31, June 30,	
	2018	2018
Accrued incentive and other compensation	\$ 217,171	\$415,182
Accrued severance payments	—	160,089
Asset retirement obligations due within one year	35,539	35,539
Accrued royalties, including suspended accounts	11,498	11,498
Accrued franchise taxes	99,000	162,805
Accrued ad valorem taxes	—	89,773
Accrued liabilities and other	\$ 363,208	\$874,886

## Note 8 — Asset Retirement Obligations

Our asset retirement obligations represent the estimated present value of the amount we expect to incur to plug, abandon and remediate our producing properties at the end of their productive lives in accordance with applicable laws. The following is a reconciliation of the beginning and ending asset retirement obligations for the six months ended December 31, 2018 and for the year ended June 30, 2018:

	December 31, June 30,	
	2018	2018
Asset retirement obligations — beginning of period	\$ 1,422,955	\$ 1,288,743
Liabilities incurred	31,268	44,700
Accretion of discount	48,962	90,290
Revision of previous estimates	—	(778 )
Asset retirement obligations — end of period	\$ 1,503,185	\$ 1,422,955
Less current portion in accrued liabilities	(35,539 )	(35,539 )
Long-term portion of asset retirement obligations	\$ 1,467,646	\$ 1,387,416

## Note 9 — Stockholders' Equity

## Common Stock

As of December 31, 2018, we had 33,186,665 shares of common stock outstanding.

The Company began paying quarterly cash dividends on common stock in December 2013. We paid dividends of \$6,634,896 and \$4,969,335 to our common stockholders during the six months ended December 31, 2018 and 2017, respectively. The following table reflects the dividends paid within the respective three month periods:

	Fiscal Year	
	2018	2017
First quarter ended September 30,	\$0.10	\$0.075
Second quarter ended December 31,	\$0.10	\$0.075

In May 2015, the Board of Directors approved a share repurchase program covering up to \$5 million of the Company's common stock. Between June 2015 and December 2015, the Company spent \$1,609,008 to repurchase 265,762 common shares at an average price of \$6.05 per share. There have been no shares repurchased in the open

market since December 2015. Under the program's terms, shares are repurchased only on the open market and in accordance with the requirements of the Securities and Exchange Commission. Such shares are initially recorded as treasury stock, then subsequently canceled. The timing and amount of repurchases depends upon several factors, including financial resources and market and business conditions. There is no fixed termination date for this repurchase program, and it may be suspended or discontinued at any time.



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Notes to Unaudited Consolidated Condensed Financial Statements

During the six months ended December 31, 2018 and 2017, the Company acquired treasury stock from holders of newly vested stock-based awards to fund the recipients' payroll tax withholding obligations. The treasury shares were subsequently canceled. Such shares were valued at fair market value on the date of vesting, as reflected in the following table:

	Six Months Ended	
	December 31,	
	2018	2017
Number of treasury shares acquired	15,489	55,018
Average cost per share	\$8.95	\$7.19
Total cost of treasury shares acquired	\$138,638	\$395,550

#### Expected Tax Treatment of Dividends

For the fiscal year ended June 30, 2018, all common dividends were treated for tax purposes as qualified dividend income to recipients. Based on our current projections for the fiscal year ending June 30, 2019, we expect all common dividends for such period to be treated as qualified dividend income. Such projections are based on our reasonable expectations as of December 31, 2018 and are subject to change based on our final tax calculations at the end of the fiscal year.

#### Note 10 — Stock-Based Incentive Plan

At the December 8, 2016 annual meeting, the stockholders approved the adoption of the Evolution Petroleum Corporation 2016 Equity Incentive Plan (the "2016 Plan"), which replaced the Evolution Petroleum Corporation Amended and Restated 2004 Stock Plan (the "2004 Plan") for which there were no shares available for future grants. The 2016 Plan authorizes the issuance of 1,100,000 shares of common stock prior to its expiration on December 8, 2026. Incentives under the 2016 Plan may be granted to employees, directors and consultants of the Company in any one or a combination of the following forms: incentive stock options and non-statutory stock options, stock appreciation rights, restricted stock awards and restricted stock unit awards, performance share awards, performance cash awards, and other forms of incentives valued in whole or in part by reference to, or otherwise based on, our common stock, including its appreciation in value. As of December 31, 2018, 852,111 shares remained available for grant under the 2016 Plan.

All outstanding awards granted under the 2004 Plan continue to be subject to the terms and conditions as set forth in the agreements evidencing such awards and the terms of the 2004 Plan. Under these agreements, we have outstanding grants of restricted common stock awards ("Restricted Stock") and contingent restricted common stock awards ("Contingent Restricted Stock") to employees and directors of the Company.

#### Restricted Stock and Contingent Restricted Stock

The Company has awarded grants of both Restricted Stock and Contingent Restricted Stock as part of its long-term incentive plan. Such grants, which expire after a maximum of four years if unvested, contain service-based, performance-based and market-based vesting provisions. The common shares underlying the Restricted Stock grants are issued on the date of grant. Contingent Restricted Stock grants vest only upon the attainment of higher performance-based or market-based vesting thresholds and are issued only upon vesting. Shares underlying Contingent Restricted Stock awards are reserved from the Plan they were granted under.

Service-based awards vest with continuous employment by the Company, generally in annual installments over their terms of three to four years. Certain awards may contain other vesting periods, including quarterly installments and one-year vesting. Restricted Stock grants which vest based on service are valued at the fair market value on the date of grant and amortized over the service period. During the six months ended December 31, 2018, we granted 31,777 service-based and 43,990 market-based Restricted Stock awards to our employees as well as 35,215 service-based awards to the Company's directors. We did not grant any performance-based awards, nor any Contingent Restricted Stock awards, during this period. The employees' service-based awards vest annually over a three-year period and the directors' service-based awards have a one-year cliff vesting period.

Performance-based grants vest upon the attainment of earnings, revenue and other operational goals and require that the recipient remain an employee or director of the Company through the vesting date. The Company recognizes compensation expense for performance-based awards ratably over the expected vesting period based on the grant date fair value when it is

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Evolution Petroleum Corporation And Subsidiaries

Notes to Unaudited Consolidated Condensed Financial Statements

deemed probable, for accounting purposes, that the performance criteria will be achieved. The expected vesting period may be deemed to be shorter than the term of the award. As of December 31, 2018, there were no performance-based awards outstanding.

Market-based awards vest if their respective two- or three-year trailing total returns on the Company's common stock exceed the corresponding total returns of various quartiles of indices consisting of either peer companies or a broad market index of companies in our industry. More recent market-based awards vest if the average of the Company's closing stock prices over defined quarterly measurement periods together with accumulated paid dividends exceeds a defined value. The fair values and expected vesting periods of these awards are determined using a Monte Carlo simulation based on the historical volatility of the Company's total return compared to the historical volatilities of the other companies in the index. Compensation expense for market-based awards is recognized over the expected vesting period using the straight-line method, so long as the holder remains an employee or director of the Company. Total compensation expense is based on the fair value of the awards at the date of grant and is independent of vesting or expiration of the awards, except for termination of service.

For market-based awards granted during the six months ended December 31, 2018, the range of assumptions used in the Monte Carlo simulation valuations, expected lives and fair values were as follows:

	Six	
	Months	
	Ended	
	December	
	31,	
	2018	
Risk-free interest rate	2.69	%
Expected life in years	2.82	
Expected volatility	41.8	%
Dividend yield	4.0	%

Unvested Restricted Stock awards at December 31, 2018 consisted of the following:

	Number of Restricted Shares	Weighted Average Grant-Date Fair Value
Service-based awards	121,265	\$ 8.62
Market-based awards	64,302	7.35
Unvested Restricted Stock at December 31, 2018	185,567	\$ 8.18

The following table sets forth the Restricted Stock transactions for the six months ended December 31, 2018:

	Number of Restricted Shares	Weighted Average Grant-Date Fair Value	Unamortized Compensation Expense at December 31, 2018	Weighted Average Remaining Amortization Period (Years)
Unvested at July 1, 2018	199,477	\$ 6.83		
Service-based shares granted	66,992	9.17		
Market-based shares granted	43,990	8.24		
Vested (124,892 )		6.57		
Unvested Restricted Stock at December 31, 2018	185,567	\$ 8.18	\$ 1,260,881	2.02

Unvested Contingent Restricted Stock awards at December 31, 2018 consisted of the following:

	Number of Contingent Restricted Shares	Weighted Average Grant-Date Fair Value
Market-based awards	10,156	\$ 3.42

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Evolution Petroleum Corporation And Subsidiaries

Notes to Unaudited Consolidated Condensed Financial Statements

The following table sets forth Contingent Restricted Stock transactions for the six months ended December 31, 2018:

	Number of Contingent Restricted Shares	Weighted Average Grant-Date Fair Value	Unamortized Compensation Expense at December 31, 2018	Weighted Average Remaining Amortization Period (Years)
Unvested at July 1, 2018	28,562	\$ 6.06		
Vested	(10,629 )	5.67		
Expired	(7,777 )	10.05		
Unvested contingent shares at December 31, 2018	10,156	\$ 3.42	\$ 6,058	.49

Stock-based compensation expense related to Restricted Stock and Contingent Restricted Stock grants for the three months ended December 31, 2018 and 2017 was \$254,111 and \$484,326, respectively. For the corresponding six month periods, stock-based compensation expense was \$469,484 and \$971,810, respectively.

## Note 11 — Income Taxes

We file a consolidated federal income tax return in the United States and various combined and separate filings in several state and local jurisdictions.

There were neither unrecognized tax benefits nor any accrued interest or penalties associated with unrecognized tax benefits during any periods presented in the financial statements. We believe we have appropriate support for the income tax positions taken and to be taken on our tax returns and that the accruals for tax liabilities are adequate for all open years based on our assessment of various factors including past experience and interpretations of tax law applied to the facts of each matter. The Company's federal and state income tax returns are open to audit under the statute of limitations for the years ended June 30, 2015 through June 30, 2018 for federal tax purposes and for the years ended June 30, 2014 through June 30, 2018 for state tax purposes. To the extent we utilize net operating losses generated in earlier years, such earlier years may also be subject to audit.

For the six months ended December 31, 2018 and 2017, respectively, we recognized income tax expense of \$2.2 million and an income tax benefit of \$(4.7) million. This benefit included a one-time \$6.0 million tax credit, resulting from adjustment of our deferred income tax liabilities at December 31, 2017 in connection with enactment of the Tax Cut and Jobs Act (the "Tax Act"). For the six months ended December 31, 2018 and 2017, the corresponding effective tax rates were 18% and (63)%. Excluding the effect of the \$6.0 million tax credit, income tax as a percentage of income before income taxes would have been approximately 19% for the six months ended December 31, 2017. Our effective tax rate will typically differ from the statutory federal rate as a result of state income taxes, primarily in the State of Louisiana, and differences related to percentage depletion in excess of basis, stock-based compensation and other permanent differences. For the six months ended December 31, 2018 and 2017, our respective statutory federal tax rates were 21% and 27.55%, as we used a blended rate during our fiscal year in which the Tax Act was enacted. The benefit of this statutory rate reduction was partially offset by a decreased benefit from depletion in excess of basis as much of our depletion carryover had been utilized in fiscal 2018.

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Evolution Petroleum Corporation And Subsidiaries  
Notes to Unaudited Consolidated Condensed Financial Statements

## Note 12 — Net Income Per Share

The following table sets forth the computation of basic and diluted income per share:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2018	2017	2018	2017
Numerator				
Net income available to common shareholders	\$3,904,565	\$9,876,848	\$9,700,366	\$12,017,380
Denominator				
Weighted average number of common shares — Basic	33,167,159	33,109,448	33,134,726	33,099,546
Effect of dilutive securities:				
Contingent restricted stock grants	9,344	30,830	13,049	40,711
Weighted average number of common shares and potentially dilutive common shares used in diluted EPS	33,176,503	33,140,278	33,147,775	33,140,257
Net income per common share — Basic	\$0.12	\$0.30	\$0.29	\$0.36
Net income per common share — Diluted	\$0.12	\$0.30	\$0.29	\$0.36

Outstanding potentially dilutive securities as of December 31, 2018 were as follows:

	Weighted Average Exercise Price	At December 31, 2018
Contingent Restricted Stock grants	\$	—10,156

Outstanding potentially dilutive securities as of December 31, 2017 were as follows:

	Weighted Average Exercise Price	At December 31, 2017
Contingent Restricted Stock grants	\$	—61,868

## Note 13 — Senior Secured Credit Agreement

On April 11, 2016, the Company entered into a three-year, senior secured reserve-based credit facility ("Facility") in an amount up to \$50 million. On May 25, 2018, we entered into the third amendment to our credit agreement governing the revolving credit facility to, among other things, extend the maturity date to April 11, 2021. On December 31, 2018, we entered into the fourth amendment to our credit agreement governing the revolving credit facility to broaden the definition for the Use of Proceeds.

As of December 31, 2018, the Company's elected commitment and borrowing base were \$40 million and we were in compliance with all financial covenants contained in the Facility. No amounts were outstanding under the Facility. Borrowings from the Facility may be used for the acquisition and development of oil and gas properties, investments in cash flow generating assets complimentary to the production of oil and gas, and for letters of credit and other general corporate purposes. Availability of borrowings under the Facility is subject to semi-annual borrowing base redeterminations.

The Facility included a placement fee of 0.50% on the initial borrowing base, amounting to \$50,000, and carries a commitment fee of 0.25% per annum on the undrawn portion of the borrowing base. Any borrowings under the Facility will bear interest, at the Company's option, at either LIBOR plus 2.75% or the Prime Rate, as defined under the Facility, plus 1.00%. The Facility contains financial covenants including a requirement that the Company

maintain, as of the last day of each fiscal quarter, (a) a maximum total leverage ratio of not more than 3.00 to 1.00, (b) a debt service coverage ratio of not less than 1.10 to 1.00, and (c) a consolidated tangible net worth of not less than \$50 million, all as defined under the Facility.

In connection with this agreement, the Company incurred \$168,972 of debt issuance costs. Such costs were capitalized in Other Assets and are being amortized to expense. The unamortized balance in debt issuance costs related to the Facility was \$34,623 as of December 31, 2018.

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Evolution Petroleum Corporation And Subsidiaries  
Notes to Unaudited Consolidated Condensed Financial Statements

Note 14 — Commitments and Contingencies

We are subject to various claims and contingencies in the normal course of business. In addition, from time to time, we receive communications from government or regulatory agencies concerning investigations or allegations of noncompliance with laws or regulations in jurisdictions in which we operate. At a minimum, we disclose such matters if we believe it is reasonably possible that a future event or events will confirm a loss through impairment of an asset or the incurrence of a liability. We accrue a loss if we believe it is probable that a future event or events will confirm a loss and we can reasonably estimate such loss and we do not accrue future legal costs related to that loss. Furthermore, we will disclose any matter that is unasserted if we consider it probable that a claim will be asserted and there is a reasonable possibility that the outcome will be unfavorable. We expense legal defense costs as they are incurred.

Lease Commitments. We have a non-cancelable operating lease for office space that expires on May 31, 2019. Future minimum lease commitments as of December 31, 2018 under this operating lease are as follows:

Twelve month periods ended December 31, 2019	\$30,447
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Rent expense for the three months ended December 31, 2018 and 2017 was \$18,726 and \$19,198, respectively. For the six months ended December 31, 2018 and 2017, rent expense was \$38,104 and \$39,049, respectively.

Note 15 — Enduro Purchase and Sale Agreement

As previously disclosed, the Company entered into a Purchase and Sale Agreement ("PSA") on May 15, 2018, to acquire, as the "stalking horse" bidder, certain oil and gas assets from an affiliate of Enduro Resource Partners LLC ("Enduro") for a purchase price of \$27.5 million, subject to the outcome of Enduro's Chapter 11 process.

Contemporaneous with executing the PSA, the Company made a \$2.75 million deposit to an acquisition escrow account which was reflected in restricted cash together with earned interest on the Company's June 30, 2018 statement of financial position. On July 20, 2018, the Company was repaid its deposit together with related earned interest as a higher bidder emerged in the Chapter 11 bidding process. In August 2018, upon the closing of a higher bidder's purchase transaction, the Company received payment of a \$1.1 million breakup fee under the terms of the PSA. This breakup fee was effectively intended to cover the Company's Enduro transaction costs, time and effort, substantially all of which occurred before June 30, 2018.



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### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis should be read in conjunction with our consolidated financial statements and notes thereto contained herein and in our Annual Report on Form 10-K for the year ended June 30, 2018 (the "Form 10-K"), along with Management's Discussion and Analysis of Financial Condition and Results of Operations contained in the Form 10-K. Any terms used but not defined herein have the same meaning given to them in the Form 10-K. Certain dollar amounts and percentages in this Management's Discussion and Analysis of Financial Condition and Results of Operations and other parts of this Quarterly Report on Form 10-Q have been rounded for presentation, and certain amounts may not sum due to rounding.

This Form 10-Q and the information referenced herein contain forward-looking statements within the meaning of the Private Securities Litigations Reform Act of 1995, Section 27A of the Securities Act of 1933 (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934. The words "plan," "expect," "project," "estimate," "assume," "believe," "anticipate," "intend," "budget," "forecast," "predict" and other similar expressions are intended to identify forward-looking statements. These statements appear in a number of places and include statements regarding our plans, beliefs or current expectations, including the plans, beliefs and expectations of our officers and directors. When considering any forward-looking statement, you should keep in mind the risk factors that could cause our actual results to differ materially from those contained in any forward-looking statement. Important factors that could cause actual results to differ materially from those in the forward-looking statements herein include the timing and extent of changes in commodity prices for oil and natural gas, operating risks and other risk factors as described in our 2018 Annual Report on Form 10-K for the year ended June 30, 2018 as filed with the Securities and Exchange Commission. Furthermore, the assumptions that support our forward-looking statements are based upon information that is currently available and is subject to change. We specifically disclaim all responsibility to publicly update any information contained in a forward-looking statement or any forward-looking statement in its entirety and therefore disclaim any resulting liability for potentially related damages. All forward-looking statements attributable to Evolution Petroleum Corporation are expressly qualified in their entirety by this cautionary statement.

We use the terms, "EPM," "Company," "we," "us" and "our" to refer to Evolution Petroleum Corporation and its wholly owned subsidiaries.

#### Executive Overview

##### General

Evolution Petroleum Corporation is an oil and gas company focused on delivering a sustainable dividend yield to its stockholders through the ownership, management and development of producing oil and gas properties. The Company's long-term goal is to build a diversified portfolio of oil and gas assets primarily through acquisition, while seeking opportunities to maintain and increase production through selective development, production enhancement and other exploitation efforts on its properties. Our largest active investment is our interest in a CO<sub>2</sub> enhanced oil recovery project in Louisiana's Delhi field.

By policy, every employee and director maintains a beneficial ownership position in our common stock. We believe this ownership helps ensure that the interests of our employees and directors are aligned with our stockholders. In May 2018, our then President and Chief Executive Officer elected to retire as of May 31, 2018. Robert Herlin, our Chairman of the Board, founder and previous CEO, was elected by the board to the position of Executive Chairman and Interim CEO. A special Transition Services Committee of the board was created with one member, William Dozier, to provide additional operational oversight to the Company during the transition to a new CEO. The Nominating and Corporate Governance Committee is working with Mr. Herlin to identify candidates and the process is expected to be completed during the quarter ending June 30, 2019.

Highlights for our Second Quarter of Fiscal 2019 and Operations Update

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"Current quarter" refers to the three months ended December 31, 2018, the Company's second quarter of fiscal 2019.

"Prior quarter" refers to the three months ended September 30, 2018, the Company's first quarter of fiscal 2019.

"Year-ago quarter" refers to the three months ended December 31, 2017, the Company's second quarter of fiscal 2018.

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### Highlights for the Quarter

We paid our twenty-first consecutive quarterly cash dividend on common shares, and declared our twenty-second quarterly dividend of \$0.10 per share payable on March 29, 2019.

Current quarter net income was \$3.9 million, or \$0.12 per diluted common share, compared to net income of \$5.8 million, or \$0.17 per diluted common share, in the prior quarter and \$9.9 million, or \$0.30 per diluted common share, in the year-ago quarter that included a \$6.0 million, or \$0.18 per diluted share, non-recurring income tax benefit related to the Tax Cuts and Jobs Act.

We reported revenues of \$11 million for the current quarter, a decrease of 10% from the prior quarter primarily due a 10% decline in realized oil price and a 40% decline in realized NGL price. The Louisiana Light Sweet ("LLS") oil price premium at Delhi increased to \$5.03 per barrel resulting in a higher realized oil price premium over the NYMEX oil price.

Total production (BOE's) grew 2% compared to the prior quarter.

General and administrative expenses were \$1.3 million for the current quarter, a 4% decrease compared to the prior quarter and a 24% decrease from the year-ago quarter.

Working capital increased 12% to \$30.8 million compared to year-ago quarter end and we remain debt free.

### Delhi Field - Enhanced Oil Recovery Project

Gross oil production at Delhi averaged 6,772 BOPD during the quarter, a 2.8% increase from the prior quarter. Gross NGL production for quarter was 983 BOEPD, down 2.9% from the prior quarter. Oil production improved quarter over quarter as we saw production from six of the new infill wells as compared to five in the prior quarter. The Company anticipates the seventh infill well will be put on production early, and the remaining two infill wells to be put on production late, in the quarter ending March 31, 2019. In addition, the operator added a third workover rig in the fiscal second quarter with positive results which also helped to improve production. Two of the infill injection wells commenced injecting CO<sub>2</sub>, contributing to an overall increase in field injection volumes from the prior quarter. We expect to see future improvement in offset wells as a result of this work. The operator continues to take steps to improve plant efficiency and minimize unplanned downtimes. We expect to see improved NGL rates this year as a result of this work.

During the current quarter, we incurred \$1.3 million on capital projects at Delhi, the majority of which, or \$0.7 million, was spent completing the drilling of a water injection well, a water source well and completing the water facilities in preparation for Phase V expansion of the flood. Additionally, \$0.3 million was expended on workovers and conformance projects, \$0.2 million on NGL plant improvements and \$0.1 million for the infill drilling program.

The current expectation for net capital spending for the remainder of the fiscal year ended June 30, 2019 is up to \$1.0 million for the ongoing infrastructure projects in advance of Phase V, the next area of field development, and various conformance and workover projects. We believe that the operator will continue the development of the field through Phase V in our fiscal year 2020. The operator has not yet announced their capital budget for calendar year 2019.

In the current quarter, operating revenues were \$11.0 million, based on an average realized oil price of \$64.37 per barrel and an average realized NGL price of \$22.46 per BOE, and we generated \$4.7 million in income from operations. The decline in NGL realized prices is directly related to the fall in oil prices in the current quarter together with the Delhi operator's ongoing fixed, per barrel post production cost allocation to the field's royalty and mineral interests which reduces our revenue from such interests. This earnings effect is partially offset by lower lease operating expense for our Delhi working interest which shares in recovered post production costs. In the year-ago quarter, operating revenues were \$10.9 million and we had income from operations of \$4.8 million, based on an average realized oil price of \$57.30 per barrel and an average realized NGL price of \$28.45 per BOE. Net production volumes in the current quarter were 2,034 barrels of oil equivalent per day ("BOEPD"), up from the 1,992 BOEPD in the prior quarter and down from the year-ago quarter's 2,215 BOEPD. Net income for the quarter was \$3.9 million, or

\$0.12 per diluted share, compared to \$5.8 million, or \$0.17 per diluted share, in the previous quarter and \$9.9 million, or \$0.30 per diluted share, in the year-ago quarter.

Additional property and project information is included under Item 1. Business, Item 2. Properties, Notes to the Financial Statements and Exhibit 99.1 of our Form 10-K for the year ended June 30, 2018. Our interests in the Delhi field consist of a 23.9% working interest (with associated 19.0% net revenue interest) and separate overriding royalty and mineral

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interests of 7.2%. This yields a total net revenue interest of 26.2%. The field is operated by Denbury Onshore LLC, a subsidiary of Denbury Resources, Inc. (the "operator").

Production costs in the Delhi field were \$3.5 million in the current quarter, down less than 1% from the prior quarter despite a 10% increase in purchased CO<sub>2</sub> volumes, largely offset by a decrease in CO<sub>2</sub> cost per mcf. Purchased CO<sub>2</sub> volumes increased 10% compared to the previous quarter and year-ago quarter to 76.3 million cubic feet (MMcf) per day due to completion of injection wells added in the 2018 infill drilling program. CO<sub>2</sub> costs were 19% higher than the year-ago quarter due to a 12% higher oil price to which CO<sub>2</sub> prices are linked and the increase in purchased CO<sub>2</sub> volumes. For six months ended December 31, 2018, CO<sub>2</sub> costs increased due to a 21% increase in price per mcf, which reflected the higher realized oil price at Delhi, together with a 5% increase in purchased volumes. The increase in other production costs was primarily attributable to higher NGL plant costs, electricity and fuel costs, increased chemicals and labor, impacted in many cases by the increased number of workover projects and the additional infill wells.

Three Months Ended December 31, 2018 and 2017

## Revenues

Compared to the year-ago quarter, current quarter revenues increased slightly due to 10% higher realized commodity prices partially offset by an 8% decrease in production volumes. The following table summarizes total production volumes, daily production volumes, average realized prices and revenue for the three months ended December 31, 2018 and 2017:

	Three Months Ended		Variance	Variance	
	2018	2017			
Oil and gas production:					
Crude oil revenues	\$10,515,875	\$10,185,635	\$330,240	3.2	%
NGL revenues	532,243	740,585	(208,342 )	(28.1)	%
Total revenues	\$11,048,118	\$10,926,220	\$121,898	1.1	%
Crude oil volumes (Bbl)	163,361	177,767	(14,406 )	(8.1)	%
NGL volumes (Bbl)	23,701	26,033	(2,332 )	(9.0)	%
Equivalent volumes (BOE)	187,062	203,800	(16,738 )	(8.2)	%
Crude oil (BOPD, net)	1,776	1,932	(156 )	(8.1)	%
NGLs (BOEPD, net)	258	283	(25 )	(8.8)	%
Equivalent volumes (BOEPD, net)	2,034	2,215	(181 )	(8.2)	%
Crude oil price per Bbl	\$64.37	\$57.30	\$7.07	12.3	%
NGL price per Bbl	22.46	28.45	(5.99 )	(21.1)	%
Equivalent price per BOE	\$59.06	\$53.61	\$5.45	10.2	%

## Production Costs

The \$0.7 million increase in production costs was due to a 29% increase in other production costs together with a 19% increase in CO<sub>2</sub> costs. The \$0.4 million increase in other production costs consisted primarily of \$0.2 million of higher fuel gas expense, increased electricity expense of \$0.1 million and workover expense of \$0.1 million.

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	Three Months Ended December 31,			
	2018	2017	Variance	Variance %
CO <sub>2</sub> costs (a)	\$1,504,930	\$1,265,582	\$239,348	18.9 %
Other production costs	1,947,238	1,508,239	438,999	29.1 %
Total production costs	\$3,452,168	\$2,773,821	\$678,347	24.5 %
CO <sub>2</sub> costs per BOE	\$8.05	\$6.21	\$1.84	29.6 %
All other production costs per BOE	10.40	7.40	3.00	40.5 %
Production costs per BOE	\$18.45	\$13.61	\$4.84	35.6 %

(a) Under our contract with the operator, purchased CO<sub>2</sub> is priced at 1% of the realized oil price in the field per Mcf, plus sales taxes of approximately 8.5% and transportation costs of \$0.20 per Mcf.

The \$0.2 million increase in CO<sub>2</sub> costs was due to an increase in purchased volumes together with an increase in unit purchase cost reflecting a higher realized oil price.

	Three Months Ended December 31,			
	2018	2017	Variance	Variance %
CO <sub>2</sub> costs per mcf	\$0.90	\$0.83	\$ 0.07	8.4 %
CO <sub>2</sub> volumes (MMcf per day, gross)	76.3	69.7	6.6	9.5 %

Calculated solely on our Delhi working interest volumes, production costs were \$25.42 per BOE, of which \$11.08 per BOE was CO<sub>2</sub> costs. These costs per equivalent barrel exclude production volumes from our royalty interests in the Delhi field, which bear almost no production costs, and are therefore higher than the rates per barrel on our total production volumes.

## Depletion, Depreciation and Amortization ("DD&amp;A")

For the current quarter DD&A was virtually flat compared to the year-ago period as the oil and gas DD&A rate increase of 5% was offset by a 8% decrease in production volumes.

	Three Months Ended December 31,			
	2018	2017	Variance	Variance %
DD&A of proved oil and gas properties	\$1,571,321	\$1,626,324	\$(55,003)	(3.4) %
Depreciation of other property and equipment	4,143	4,153	(10)	—
Amortization of intangibles	3,391	3,391	—	— %
Accretion of asset retirement obligations	24,778	23,023	1,755	7.6 %
Total DD&A	\$1,603,633	\$1,656,891	\$(53,258)	(3.2) %
Oil and gas DD&A rate per BOE	\$8.40	\$7.98	\$0.42	5.3 %

## General and Administrative Expenses

Expenses for the current quarter decreased \$0.4 million, or 24%, to \$1.3 million from the year-ago quarter due to lower expenses of \$0.3 million for incentive bonuses and stock compensation, \$0.1 million for litigation expense and \$0.1 million of acquisition due diligence costs, partially offset by \$0.1 million of higher current quarter board compensation expenses.



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## Other Income and Expenses

Other income and expense (net) increased due higher interest income partially offset by increased interest expense.

	Three Months Ended December 31,			
	2018	2017	Variance	Variance %
Interest and other income	\$59,858	\$15,841	\$44,017	277.9 %
Interest expense	(29,345 )	(20,456 )	(8,889 )	43.5 %
Total other income, net	\$30,513	\$(4,615 )	\$35,128	n.m.

n. m. Not meaningful.

## Net Income

Although income before income taxes for the three months ended December 31, 2018 was essentially flat compared to the year-ago quarter, net income available to common stockholders decreased \$6.0 million, or 60%, compared to the year-ago quarter which included a non-recurring \$6.0 million deferred tax credit. This income tax benefit resulted from the revaluation of our deferred income tax liabilities at December 31, 2017 to reflect a lower federal statutory rate under the Tax Cut and Jobs Act. Excluding this tax benefit, income taxes as a percentage of income before income taxes would have been approximately 21% for the year-ago quarter.

	Three Months Ended December 31,			
	2018	2017	Variance	Variance %
Income before income taxes	\$4,764,260	\$4,824,637	\$(60,377 )	(1 )%
Income tax provision (benefit)	859,695	(5,052,211 )	5,911,906	(117 )%
Net income available to common stockholders	\$3,904,565	\$9,876,848	\$(5,972,283 )	(60 )%
Income tax provision (benefit) as a percentage of income before income taxes	18	% (105 )	%	%



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Six Months Ended December 31, 2018 and 2017

## Revenues

Compared to the corresponding year-ago period, current period revenues increased 21% due to 29% higher realized commodity prices partially offset by a 6% decrease in production volumes. The following table summarizes total production volumes, daily production volumes, average realized prices and revenue for the six months ended December 31, 2018 and 2017:

	Six Months Ended December 31,		Variance	Variance	
	2018	2017		%	
Oil and gas production:					
Crude oil revenues	\$21,913,327	\$18,014,890	\$3,898,437	21.6	%
NGL revenues	1,441,870	1,313,297	128,573	9.8	%
Total revenues	\$23,355,197	\$19,328,187	\$4,027,010	20.8	%
Crude oil volumes (Bbl)	322,267	344,504	(22,237)	(6.5)	%
NGL volumes (Bbl)	48,102	51,279	(3,177)	(6.2)	%
Equivalent volumes (BOE)	370,369	395,783	(25,414)	(6.4)	%
Crude oil (BOPD, net)	1,751	1,872	(121)	(6.5)	%
NGLs (BOEPD, net)	261	279	(18)	(6.5)	%
Equivalent volumes (BOEPD, net)	2,012	2,151	(139)	(6.5)	%
Crude oil price per Bbl	\$68.00	\$52.29	\$15.71	30.0	%
NGL price per Bbl	29.98	25.61	4.37	17.1	%
Equivalent price per BOE	\$63.06	\$48.84	\$14.22	29.1	%

## Production Costs

The \$1.4 million increase in production costs was due to a 23% increase in other production costs together with a 27% increase in CO<sub>2</sub> costs. The \$0.7 million increase in other production costs consisted primarily of \$0.2 million of higher NGL plant expense, \$0.1 million of fuel gas expense, increased electricity expense of \$0.1 million, of \$0.1 million of higher labor, \$0.1 million for chemicals and increased workover expense of \$0.1 million.

	Six Months Ended December 31,		Variance	Variance	
	2018	2017		%	
CO <sub>2</sub> costs (a)	\$2,988,782	\$2,353,843	\$634,939	27.0	%
Other production costs	3,921,816	3,175,660	746,156	23.5	%
Total production costs	\$6,910,598	\$5,529,503	\$1,381,095	25.0	%
CO <sub>2</sub> costs per BOE	\$8.07	\$5.95	\$2.12	35.6	%
All other production costs per BOE	10.59	8.02	2.57	32.0	%
Production costs per BOE	\$18.66	\$13.97	\$4.69	33.6	%

(a) Under our contract with the operator, purchased CO<sub>2</sub> is priced at 1% of the realized oil price in the field per Mcf, plus sales taxes of approximately 8.5% and transportation costs of \$0.20 per Mcf.

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The \$0.6 million increase in CO<sub>2</sub> costs was due to a 5% increase in purchased volumes together with a 21% increase in price reflecting higher realized oil price.

	Six Months Ended December 31,			
	2018	2017	Variance	Variance %
CO <sub>2</sub> costs per mcf	\$0.93	\$0.77	\$ 0.16	20.8 %
CO <sub>2</sub> volumes (MMcf per day, gross)	72.9	69.5	3.4	4.9 %

Calculated solely on our Delhi working interest volumes, production costs were \$25.70 per BOE, of which \$11.11 per BOE was CO<sub>2</sub> costs. These costs per equivalent barrel exclude production volumes from our royalty interests in the Delhi field, which bear almost no production costs, and are therefore higher than the rates per barrel on our total production volumes.

## Depletion, Depreciation and Amortization ("DD&amp;A")

DD&A expense was virtually flat compared to the same year-ago period as the oil and gas DD&A rate increase of 5% was offset by a 6% decrease in production volumes.

	Six Months Ended December 31,			
	2018	2017	Variance	Variance %
DD&A of proved oil and gas properties	\$3,088,063	\$3,137,205	\$(49,142)	(1.6)%
Depreciation of other property and equipment	8,286	8,424	(138)	(1.6)%
Amortization of intangibles	6,782	6,782	—	—%
Accretion of asset retirement obligations	48,962	44,602	4,360	9.8%
Total DD&A	\$3,152,093	\$3,197,013	\$(44,920)	(1.4)%

Oil and gas DD&A rate per BOE	\$8.34	\$7.93	\$0.41	5.2%
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## General and Administrative Expenses

Expenses for the six months ended December 31, 2018 decreased \$0.7 million, or 21%, to \$2.6 million from the same year-ago period due to lower stock and incentive compensation of \$0.6 million, a \$0.1 million decrease in litigation and \$0.2 million of lower severance benefits and other G&A expense, partially offset by \$0.2 million of higher board compensation expenses during the six months ended December 31, 2018.

## Other Income and Expenses

Other income and expense (net) increased due primarily to the Enduro breakup fee received during August 2018.

	Six Months Ended December 31,			
	2018	2017	Variance	Variance %
Enduro transaction breakup fee	1,100,000	—	1,100,000	n.m.
Interest and other income	106,429	30,691	75,738	246.8%
Interest expense	(58,690)	(40,911)	(17,779)	43.5%
Total other income, net	\$1,147,739	\$(10,220)	\$1,157,959	n.m.

n. m. Not meaningful.

## Net Income

Net income available to common stockholders for the six months ended December 31, 2018 decreased \$2.3 million, or 19%, to \$9.7 million compared to the same year-ago period primarily due to a non-recurring prior year deferred tax credit of \$6.0 million, partially offset by a \$4.5 million, or 61%, increase in income before income taxes. This income tax benefit resulted from the revaluation of our deferred income tax liabilities at December 31, 2017 to reflect the

lower federal statutory

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rate under the Tax Cut and Jobs Act.

	Six Months Ended December 31,			
	2018	2017	Variance	Variance %
Income before income taxes	11,876,413	7,355,491	4,520,922	61.5 %
Income tax provision (benefit)	2,176,047	(4,661,889 )	6,837,936	(146.7)%
Net income available to common stockholders	\$9,700,366	\$12,017,380	\$(2,317,014)	(19.3 )%
Income tax provision as a percentage of income before income taxes	18	% (63	)%	

Excluding the effect of the \$6.0 million tax benefit from income taxes for the six months ended December 31, 2017, income tax as a percentage of income before income taxes would have been approximately 19%. For the six months ended December 31, 2018 and 2017, our respective statutory federal tax rates were 21% and 27.55%, as we used a blended rate during our fiscal 2018 in which the Tax Cut and Jobs Act was enacted. The benefit of the lower statutory rate was partially offset by a decreased benefit from depletion in excess of basis as much of our depletion carryover had been utilized by June 30, 2018.

#### Liquidity and Capital Resources

We had \$30.0 million in cash and cash equivalents (and no restricted cash) at December 31, 2018 and \$27.7 million of cash, cash equivalents and restricted cash at June 30, 2018.

In addition, we have a senior secured reserve-based credit facility (the "Facility") with a maximum capacity of \$50 million. The Facility had \$40 million of undrawn borrowing base availability on December 31, 2018. There have been no borrowings under the Facility, which matures on April 11, 2021 and is secured by substantially all of the Company's assets.

In the current quarter, we amended the credit agreement to broaden the definition for Use of Proceeds to provide funds, limited to an amount not in excess of 25% of the borrowing base, for investments into cash flow generating assets complimentary to the production of oil and gas.

Any future borrowings bear interest, at the Company's option, at either LIBOR plus 2.75% or the Prime Rate, as defined under the Facility, plus 1.0%. The Facility contains covenants that require the maintenance of (i) a total leverage ratio of not more than 3.0 to 1.0, (ii) a debt service coverage ratio of not less than 1.1 to 1.0 and (iii) a consolidated tangible net worth of not less than \$50.0 million, each as defined in the Facility. The Facility also contains other customary affirmative and negative covenants and events of default. As of December 31, 2018, the Company was in compliance with all covenants contained in the Facility.

During the six months ended December 31, 2018, we funded our operations, capital expenditures and cash dividends with cash generated from operations resulting in an increase of \$2.3 million in cash. As of December 31, 2018, our working capital was \$30.8 million, an increase of \$3.1 million over working capital of \$27.7 million at June 30, 2018. We have historically funded our operations through cash from operations and working capital. Our primary source of cash is the sale of oil and natural gas liquids production. A portion of these cash flows are used to fund our capital expenditures. While we expect to continue to expend capital to further develop the Delhi field, we and the operator have flexibility as to when this capital is spent. The Company expects to manage future development activities in the Delhi field within the boundaries of its operating cash flow and existing working capital.

We may choose to pursue new growth opportunities through acquisitions or other transactions. In addition to our cash on hand, we have access to at least \$40 million of undrawn elected borrowing base availability under our senior secured credit facility. In addition we have an effective shelf registration statement with Securities and Exchange Commission under which we may issue up to \$500 million of new debt or equity securities. If we choose to pursue new growth opportunities, we would expect to use our internal resources of cash, working capital and borrowing capacity under our credit facility. It may also be advantageous for us to consider issuing additional equity as part of any potential transaction, but we have no specific plans to issue additional equity at this time.

Our other significant use of cash is our on-going dividend program. The Board of Directors instituted a cash dividend on our common stock in December 2013 and we have since paid twenty-one consecutive quarterly dividends.

Distribution of a substantial portion of free cash flow in excess of our operating and capital requirements through cash dividends and potential repurchases of our common stock remains a priority of our financial strategy, and it is our long term goal to increase our dividends over time as appropriate. On February 5, 2019, the Board declared the next quarterly common stock dividend of \$0.10 per share, which will be paid on March 29, 2019 to stockholders of record on March 15, 2019. The Board reviews the

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quarterly dividend rate in light of our financial position and operations, forecasted results, including the outlook for oil and NGL prices, the timing of further expansion of Delhi development and other potential growth opportunities.

**Capital Budget - Delhi Field**

During the six months ended December 31, 2018, we incurred \$4.0 million of capital expenditures at Delhi. Our current expectations for net capital spending for the remainder of the fiscal year ended June 30, 2019 is up to to \$1.0 million for continuation of Phase V infrastructure projects and various conformance and workover projects, which represent carryover projects approved from 2018. The operator has not yet announced their capital budget plans for 2019, however we anticipate funding for our share of capital expenditure at Delhi to be met from cash flows from operations.

Our proved undeveloped reserves at June 30, 2018 included 537 MBOE of reserves and \$1.9 million of future development costs associated with the infill drilling program and 1,546 MBOE of reserves and \$10.9 million of future development costs associated with Phase V development in the eastern portion of the field. The timing of Phase V development is dependent in part on the results and CO<sub>2</sub> requirements of the infill drilling program. The timing of such development is also dependent, in part, on the field operator's available funds and capital spending plans and priorities within its portfolio of properties. At present, we expect to begin this development in our fiscal year 2020. Funding for our anticipated capital expenditures at Delhi for our fiscal 2020 is expected to be met from cash flows from operations and current working capital.

**Overview of Cash Flow Activities**

The table below compares a summary of our condensed consolidated statements of cash flows for six months ended December 31, 2018 and 2017 presented on page 4 of this report on Form 10-Q.

	Six Months Ended December 31,		
Increases (Decreases) in Cash:	2018	2017	Difference
	(In Millions)		
Net cash provided by operating activities	\$14.1	\$9.1	\$ 5.0
Net cash used in investing activities	(5.0 )	(1.0 )	(4.0 )
Net cash used in financing activities	(6.8 )	(5.4 )	(1.4 )
	\$2.3	\$2.7	\$ (0.4 )

Cash provided by operating activities in the current year period was \$5.0 million more than the same year-ago period due to a \$5.1 million increase in cash provided by non-cash expenses and a \$2.2 million increase in cash provided from current operating assets and liabilities, partially offset by \$2.3 million of lower current period net income. The year-ago period non-cash items used, rather than provided cash, because of a one-time \$6.0 million deferred income tax credit related to enactment of the Tax Cut and Jobs Act.

Cash used in investing activities increased \$4.0 million primarily due to higher capital expenditure disbursements in the 2019 period.

Cash used by financing activities increased \$1.4 million due to \$1.7 million of increased cash dividends, reflecting an higher quarterly dividend rate of \$0.10 per share in the 2019 period compared to \$0.075 per share during the first half of fiscal 2018, partially offset by \$0.3 million of lower common share repurchases in connection with stock-based awards vestings.

**Recently Adopted and Recently Issued Accounting Pronouncements**

See "Note 2 – Summary of Significant Accounting Policies" for discussion of the pronouncements we recently adopted as well as the recently issued accounting pronouncements from the Financial Accounting Standards Board.

**Other Economic Factors**

**Inflation.** Although the general inflation rate in the United States, as measured by the Consumer Price Index and the Producer Price Index, has been relatively low in recent years, the oil and gas industry has experienced unusually volatile price movements in commodity prices, vendor goods and oilfield services. Prices for drilling and oilfield services, oilfield equipment, tubulars, labor, expertise and other services impact our lease operating expenses and our

capital expenditures. During fiscal 2019 to date, we have seen a firming of prices for operating and capital costs as a result of improving demand and a closer balance with the supply of goods and services in the industry. Product prices, operating costs and development costs may not always move in tandem.

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**Known Trends and Uncertainties.** General worldwide economic conditions, as well as economic conditions for the oil and gas industry specifically, continue to be uncertain and volatile. Concerns over uncertain future economic growth are affecting numerous industries and companies, as well as consumers, which impact demand for crude oil and natural gas. If the supply of crude oil and natural gas exceeds demand in the future, it may put downward pressure on crude oil and natural gas prices, thereby lowering our revenues, profits, cash flow and working capital going forward. **Seasonality.** Our business is generally not directly seasonal, except for instances when weather conditions may adversely affect access to our properties or delivery of our petroleum products. Although we do not generally modify our production for changes in market demand, we do occasionally experience seasonality in the product prices we receive, driven by summer cooling and driving, winter heating, and extremes in seasonal weather, including hurricanes. We have also experienced adverse impacts on our production from very high summer temperatures and extremely cold winter weather.

### **Off Balance Sheet Arrangements**

The Company had no off-balance sheet arrangements to report for the quarter ended December 31, 2018.

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

Information about market risks for the three months ended December 31, 2018, did not change materially from the disclosures in Item 7A of our Annual Report on Form 10-K for the year ended June 30, 2018.

#### **Commodity Price Risk**

Our most significant market risk is the pricing for crude oil and NGL's. We expect energy prices to remain volatile and unpredictable. If energy prices decline significantly, our revenues and cash flow would significantly decline. In addition, a non-cash write-down of our oil and gas properties could be required under full cost accounting rules if future oil and gas commodity prices sustained a significant decline. Prices also affect the amount of cash flow available for capital expenditures and our ability to borrow and raise additional capital, as, if and when needed. We may use derivative instruments to manage our exposure to commodity price risk from time to time based on our assessment of such risk.

#### **Interest Rate Risk**

We currently have only a small exposure to changes in interest rates. Changes in interest rates affect the interest earned on our cash and cash equivalents. Under our current policies, we do not use interest rate derivative instruments to manage exposure to interest rate changes.

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

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to this Company's management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow for timely decisions regarding required disclosure.

As required by Securities and Exchange Commission Rule 13a-15(b), we carried out an evaluation, under the supervision and with the participation of the Company's management, including our Interim Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(c) and 15d-15(e)) as of the end of the quarter covered by this report. In designing and evaluating our disclosure controls and procedures, our management recognizes that controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving desired control objectives. Based on the foregoing, our Interim Chief Executive Officer and Chief Financial Officer concluded that as of December 31, 2018 our disclosure controls and procedures are effective in ensuring that the information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms.

Under the supervision and with the participation of the Company's management, including its Interim Chief Executive Officer and Chief Financial Officer, during the quarter ended December 31, 2018, we have determined there has been no changes in our internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.





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## PART II - OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS

None.

## ITEM 1A. RISK FACTORS

Our Annual Report on Form 10-K for the year ended June 30, 2018 includes a detailed description of our risk factors. There have been no material changes to the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended June 30, 2018.

## ITEM 2. UNREGISTERED SALE OF EQUITY SECURITIES AND USE OF PROCEEDS

## Issuer Purchases of Equity Securities

During the quarter ended December 31, 2018, the Company received shares of common stock from employees of the Company to pay their share of payroll taxes arising from vestings of restricted stock and contingent restricted stock. During this quarter, the Company did not purchase any common stock in the open market under the previously announced share repurchase program. The table below summarizes information about the Company's purchases of its equity securities during the quarter ended December 31, 2018.

Period	(a) Total Number of Shares Purchased (1)	(b) Average Price Paid per Share(1)	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (2)	(d) Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (2)
October 2018	—	\$—	Not applicable	\$3.4 million
November 2018	—	\$—	Not applicable	\$3.4 million
December 2018	6,402	\$7.60	Not applicable	\$3.4 million
Total	6,402	\$7.60	Not applicable	\$3.4 million

(1)During the current quarter the Company received shares of common stock from certain of its employees which were surrendered in exchange for their payroll tax liabilities arising from vestings of restricted stock and contingent restricted stock. The acquisition cost per share reflects the weighted-average market price of the Company's shares on the dates vested.

(2)On May 12, 2015, the Board of Directors approved a share repurchase program covering up to \$5 million of the Company's common stock. Under the program's terms, shares may be repurchased only on the open market and in accordance with the requirements of the Securities and Exchange Commission. The timing and amount of repurchases will depend upon several factors, including financial resources and market and business conditions. There is no fixed termination date for this repurchase program, and the repurchase program may be suspended or discontinued at any time. Such shares are initially recorded as treasury stock, then subsequently canceled.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

## ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

## ITEM 5. OTHER INFORMATION

None.



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ITEM 6. EXHIBITS

- A. Exhibits
- 10.1 Fourth Amendment to Credit Agreement dated April 11, 2016, between Evolution Petroleum Corporation and Midfirst Bank effective December 31, 2018 (filed herewith)
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) under the Securities Exchange Act of 1934, as amended.
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) under the Securities Exchange Act of 1934, as amended.
- 32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS XBRL Instance Document
- 101.SCH XBRL Taxonomy Extension Schema Document
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

SIGNATURES

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

EVOLUTION PETROLEUM CORPORATION  
(Registrant)

By: /s/ DAVID JOE  
David Joe  
Senior Vice President, Chief Financial Officer and  
Treasurer

Date: February 8, 2019