

DOWNEY FINANCIAL CORP

Form 10-Q

May 03, 2006

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended **March 31, 2006**

OR

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 **1-13578**

DOWNEY FINANCIAL CORP.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

33-0633413

(I.R.S. Employer Identification No.)

3501 Jamboree Road, Newport Beach, CA

(Address of principal executive office)

92660

(Zip Code)

Registrant's telephone number, including area code

(949) 854-0300

N/A

(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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated file Accelerated filer Non-accelerated filer

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

At March 31, 2006, 27,853,783 shares of the Registrant's Common Stock, \$0.01 par value were outstanding.

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DOWNEY FINANCIAL CORP.

March 31, 2006 QUARTERLY REPORT ON FORM 10-Q

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PART I FINANCIAL INFORMATION**ITEM 1. FINANCIAL STATEMENTS****DOWNEY FINANCIAL CORP. AND SUBSIDIARIES****Consolidated Balance Sheets**

(Dollars in Thousands, Except Per Share Data)

March 31, December 31, March 31,
2006 2005 2005

Assets

Cash	\$ 168,822	\$ 190,396	\$ 133,621
Federal funds	-	-	10,003

Cash and cash equivalents	168,822	190,396	143,624
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U.S. Treasury, government sponsored entities and other investment securities

available for sale, at fair value	730,402	626,313	511,703
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Loans held for sale, at lower of cost or fair value	561,511	464,488	1,279,734
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Mortgage-backed securities available for sale, at fair value	271	277	296
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Loans held for investment	15,912,318	15,391,759	14,485,191
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Allowance for loan losses	(44,504)	(34,601)	(35,072)
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Loans held for investment, net	15,867,814	15,357,158	14,450,119
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Investments in real estate and joint ventures	49,182	49,344	56,964
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Real estate acquired in settlement of loans	385	908	2,783
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Premises and equipment	110,595	109,574	105,596
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Federal Home Loan Bank stock, at cost	182,557	179,844	243,613
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Mortgage servicing rights, net	20,165	20,302	19,610
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Other assets	111,055	97,059	80,936
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	\$ 17,802,759	\$ 17,095,663	\$ 16,894,978
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Liabilities and Stockholders Equity

Deposits	\$ 12,198,903	\$ 11,876,848	\$ 10,309,077
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Federal Home Loan Bank advances	3,825,811	3,557,515	5,093,874
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Senior notes	198,129	198,087	197,964
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Accounts payable and accrued liabilities	189,552	114,527	118,649
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Deferred income taxes	140,961	140,467	121,078
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Total liabilities	16,553,356	15,887,444	15,840,642
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Stockholders equity

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Preferred stock, par value of \$0.01 per share; authorized
5,000,000 shares;

outstanding none	-	-	-
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Common stock, par value of \$0.01 per share; authorized
50,000,000 shares;

issued 28,235,022 shares at March 31, 2006,
December 31, 2005 and

March 31, 2005; outstanding 27,853,783 shares at
March 31, 2006,

December 31, 2005 and March 31, 2005	282	282	282
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Additional paid-in capital	93,792	93,792	93,792
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Accumulated other comprehensive loss	(6,196)	(5,408)	(1,951)
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Retained earnings	1,178,317	1,136,345	979,005
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Treasury stock, at cost, 381,239 shares at March 31,
2006,

December 31, 2005 and March 31, 2005	(16,792)	(16,792)	(16,792)
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Total stockholders equity	1,249,403	1,208,219	1,054,336
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	\$ 17,802,759	\$ 17,095,663	\$ 16,894,978
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See accompanying notes to consolidated financial statements.

DOWNEY FINANCIAL CORP. AND SUBSIDIARIES**Consolidated Statements of Income**

*Three Months Ended
March 31,*

(Dollars in Thousands, Except Per Share Data)

	2006	2005
Interest income		
Loans	\$ 255,345	\$ 183,910
U.S. Treasury and government sponsored entities securities	7,336	4,838
Mortgage-backed securities	3	3
Other investment securities	2,279	2,538
Total interest income	264,963	191,289
Interest expense		
Deposits	91,835	49,023
Federal Home Loan Bank advances	43,914	33,980
Senior notes	3,298	3,295
Total interest expense	139,047	86,298
Net interest income	125,916	104,991
Provision for credit losses	10,057	2,038
Net interest income after provision for credit losses	115,859	102,953
Other income, net		
Loan and deposit related fees	8,558	8,604
Real estate and joint ventures held for investment, net	2,289	2,580
Secondary marketing activities:		
Loan servicing income, net	189	1,484
Net gains on sales of loans and mortgage-backed securities	11,654	30,615
Net gains on sales of mortgage servicing rights	-	981
Net gains on sales of investment securities	-	27
Other	520	520
Total other income, net	23,210	44,811
Operating expense		
Salaries and related costs	40,780	39,155
Premises and equipment costs	8,538	8,000
Advertising expense	1,242	1,350

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SAIF insurance premiums and regulatory assessments	1,014	927
Professional fees	792	336
Other general and administrative expense	9,175	8,392
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Total general and administrative expense	61,541	58,160
Net operation of real estate acquired in settlement of loans	(9)	64
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Total operating expense	61,532	58,224
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Income before income taxes	77,537	89,540
Income taxes	32,780	37,801
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Net income	\$ 44,757	\$ 51,739
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Per share information		
Basic	\$ 1.61	\$ 1.86
Diluted	\$ 1.61	\$ 1.86
Cash dividends declared and paid	\$ 0.10	\$ 0.10
Weighted average shares outstanding		
Basic	27,853,783	27,853,783
Diluted	27,883,221	27,881,839
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See accompanying notes to consolidated financial statements.

DOWNEY FINANCIAL CORP. AND SUBSIDIARIES**Consolidated Statements of Comprehensive Income**

*Three Months Ended
March 31,*

(In Thousands)

	2006	2005
Net income	\$ 44,757	\$ 51,739
Other comprehensive income (loss), net of income taxes (benefits)		
Unrealized gains (losses) on securities available for sale:		
U.S. Treasury, government sponsored entities and other investment		
securities available for sale, at fair value	(1,367)	(2,443)
Mortgage-backed securities available for sale, at fair value	-	-
Reclassification of realized amounts included in net income	-	(17)
Unrealized gains (losses) on cash flow hedges:		
Net derivative instruments	503	(78)
Reclassification of realized amounts included in net income	76	269
Total other comprehensive loss, net of income tax benefits	(788)	(2,269)
Comprehensive income	\$ 43,969	\$ 49,470

See accompanying notes to consolidated financial statements.

DOWNEY FINANCIAL CORP. AND SUBSIDIARIES**Consolidated Statements of Cash Flows**

Three Months Ended
March 31,

(In Thousands)

2006

2005

Cash flows from operating activities

Net income	\$ 44,757	\$ 51,739
Adjustments to reconcile net income to net cash used for operating activities:		
Depreciation	3,285	3,309
Amortization	26,076	16,630
Provision for losses on loans, loan-related commitments, investments, real estate and joint ventures, mortgage servicing rights, real estate acquired in settlement of loans, and other assets	10,018	835
Net gains on sales of loans and mortgage-backed securities, mortgage servicing rights, investment securities, real estate and other assets	(12,618)	(33,092)
Interest capitalized on loans (negative amortization)	(64,827)	(18,707)
Federal Home Loan Bank stock dividends	(2,274)	-
Loans originated and purchased for sale	(980,164)	(2,181,392)
Proceeds from sales of loans held for sale, including those sold as mortgage-backed securities	887,037	2,059,786
Other, net	(18,877)	(48,432)
Net cash used for operating activities	(107,587)	(149,324)

Cash flows from investing activities

Proceeds from sales of:		
Wholly owned real estate and real estate acquired in settlement of loans	681	663
Proceeds from maturities or calls of U.S. Treasury, government sponsored entities and other investment securities available for sale	4,750	8,100
Purchase of:		
U.S. Treasury, government sponsored entities and other investment securities available for sale	(61,225)	(27,044)
Loans held for investment	(12,218)	(25,360)
Premises and equipment	(9,902)	(4,673)
Federal Home Loan Bank stock	(439)	-
Originations of loans held for investment (net of refinances of \$199,203 for the three months ended March 31, 2006 and \$166,659 for the three months ended March 31, 2005)	(1,621,617)	(1,876,331)
Principal payments on loans held for investment and mortgage-backed securities available for sale	1,194,760	876,996
Net change in undisbursed loan funds	(2,881)	36,450
Investments in real estate held for investment	1,051	(136)

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Other, net	5,445	2,175
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Net cash used for investing activities	(501,595)	(1,009,160)
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See accompanying notes to consolidated financial statements.

DOWNEY FINANCIAL CORP. AND SUBSIDIARIES**Consolidated Statements of Cash Flows (Continued)**

Three Months Ended
March 31,

(In Thousands)

2006

2005

Cash flows from financing activities

Net increase in deposits	\$ 322,055	\$ 651,099
Proceeds from Federal Home Loan Bank advances	7,148,170	10,558,350
Repayments of Federal Home Loan Bank advances	(6,877,100)	(10,015,350)
Cash dividends	(2,785)	(2,785)