Walker & Dunlop, Inc.
Form 10-Q
August 02, 2017

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 June 30, 2017

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: 001-35000

Walker & Dunlop, Inc.

(Exact name of registrant as specified in its charter)

Maryland	80-0629925
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

7501 Wisconsin Avenue, Suite 1200E

Bethesda, Maryland 20814

(301) 215-5500

(Address of principal executive offices and 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
		(Do not check if a smaller reporting company)
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.

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

As of July 26, 2017, there were 31,246,830 total shares of common stock outstanding.

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PART I

FINANCIAL INFORMATION

Item 1. Financial Statements

Walker & Dunlop, Inc. and Subsidiaries

Condensed Consolidated Balance Sheets

(In thousands, except per share data)

	June 30, 2017 (unaudited)	December 31, 2016
Assets		
Cash and cash equivalents	$ 53,338	$ 118,756
Restricted cash	15,768	9,861
Pledged securities, at fair value	92,401	84,850
Loans held for sale, at fair value	1,608,025	1,858,358
Loans held for investment, net	167,540	220,377
Servicing fees and other receivables, net	34,794	29,459
Derivative assets	24,991	61,824
Mortgage servicing rights	573,159	521,930
Goodwill and other intangible assets	124,621	97,372
Other assets	71,398	49,645
Total assets	$ 2,766,035	$ 3,052,432
Liabilities		
Accounts payable and other liabilities	$ 229,471	$ 232,231
Performance deposits from borrowers	14,894	10,480
Derivative liabilities	500	4,396
Guaranty obligation, net of accumulated amortization	36,492	32,292
Allowance for risk-sharing obligations	3,648	3,613
Warehouse notes payable	1,630,268	1,990,183
Note payable	164,011	164,163
Total liabilities	$ 2,079,284	$ 2,437,358
Equity		
Preferred shares, Authorized 50,000, none issued.	$ —	$ —
Common stock, $0.01 par value. Authorized 200,000; issued and outstanding 30,144 shares at June 30, 2017 and 29,551 shares at December 31, 2016	301	296
Additional paid-in capital	222,989	228,889
Retained earnings	458,819	381,031
Total stockholders' equity	$ 682,109	$ 610,216
Noncontrolling interests	4,642	4,858

Total equity	$ 686,751	$ 615,074
Commitments and contingencies (NOTE 10)	—	—
Total liabilities and equity	$ 2,766,035	$ 3,052,432

See accompanying notes to condensed consolidated financial statements.

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Walker & Dunlop, Inc. and Subsidiaries

Condensed Consolidated Statements of Income

(In thousands, except per share data)

(Unaudited)

	For the three months ended June 30,		For the six months ended June 30,	
	2017	2016	2017	2016
Revenues				
Gains from mortgage banking activities	$ 102,176	$ 102,453	$ 198,608	$ 148,776
Servicing fees	43,214	32,771	84,739	64,420
Net warehouse interest income	5,800	3,580	12,420	10,311
Escrow earnings and other interest income	4,514	1,955	7,806	3,595
Other	10,703	7,099	21,346	14,997
Total revenues	$ 166,407	$ 147,858	$ 324,919	$ 242,099
Expenses				
Personnel	$ 63,516	$ 55,758	$ 119,688	$ 89,988
Amortization and depreciation	32,860	26,425	65,198	51,580
Provision (benefit) for credit losses	(93)	292	(225)	(117)
Interest expense on corporate debt	2,443	2,465	4,846	4,934
Other operating expenses	11,599	11,212	23,207	19,826
Total expenses	$ 110,325	$ 96,152	$ 212,714	$ 166,211
Income from operations	$ 56,082	$ 51,706	$ 112,205	$ 75,888
Income tax expense	21,570	19,595	34,633	28,444
Net income before noncontrolling interests	$ 34,512	$ 32,111	$ 77,572	$ 47,444
Less: net income (loss) from noncontrolling interests	(55)	90	(216)	(35)
Walker & Dunlop net income	$ 34,567	$ 32,021	$ 77,788	$ 47,479
Basic earnings per share	$ 1.15	$ 1.09	$ 2.60	$ 1.61
Diluted earnings per share	$ 1.08	$ 1.05	$ 2.43	$ 1.55
Basic weighted average shares outstanding	30,131	29,388	29,971	29,438
Diluted weighted average shares outstanding	32,097	30,627	32,067	30,714

See accompanying notes to condensed consolidated financial statements.

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Walker & Dunlop, Inc. and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Six Months Ended June 30, 2017	2016
Cash flows from operating activities		
Net income before noncontrolling interests	$ 77,572	$ 47,444
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Gains attributable to the fair value of future servicing rights, net of guaranty obligation	(90,204)	(79,496)
Change in the fair value of premiums and origination fees	1,921	(11,954)
Amortization and depreciation	65,198	51,580
Provision (benefit) for credit losses	(225)	(117)
Other operating activities, net	365,842	339,053
Net cash provided by (used in) operating activities	$ 420,104	$ 346,510
Cash flows from investing activities		
Capital expenditures	$ (2,049)	$ (777)
Funding of preferred equity investments	(11,385)	(6,409)
Net cash paid to increase ownership interest in a previously held equity-method investment	—	(1,058)
Acquisitions, net of cash received	(15,000)	—
Purchase of mortgage servicing rights	—	(43,374)
Originations of loans held for investment	(167,079)	(141,842)
Principal collected on loans held for investment	100,980	133,120
Net cash provided by (used in) investing activities	$ (94,533)	$ (60,340)
Cash flows from financing activities		
Borrowings (repayments) of warehouse notes payable, net	$ (414,266)	$ (333,615)
Borrowings of interim warehouse notes payable	128,660	98,863
Repayments of interim warehouse notes payable	(75,615)	(97,873)
Repayments of note payable	(552)	(552)
Proceeds from issuance of common stock	2,885	3,291
Repurchase of common stock	(17,590)	(11,979)
Debt issuance costs	(1,053)	(1,689)
Distributions to noncontrolling interests	—	(5)
Net cash provided by (used in) financing activities	$ (377,531)	$ (343,559)
Net increase (decrease) in cash, cash equivalents, restricted cash, and restricted cash equivalents (NOTE 2)	$ (51,960)	$ (57,389)

Cash, cash equivalents, restricted cash, and restricted cash equivalents at beginning of period	213,467	214,484
Total of cash, cash equivalents, restricted cash, and restricted cash equivalents at end of period	$ 161,507	$ 157,095
Supplemental Disclosure of Cash Flow Information:		
Cash paid to third parties for interest	$ 22,513	$ 18,008
Cash paid for income taxes	27,748	16,426

See accompanying notes to condensed consolidated financial statements.

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NOTE 1—ORGANIZATION AND BASIS OF PRESENTATION

These financial statements represent the condensed consolidated financial position and results of operations of Walker & Dunlop, Inc. and its subsidiaries. Unless the context otherwise requires, references to "we," "us," "our," "Walker & Dunlop" and the "Company" mean the Walker & Dunlop consolidated companies. The statements have been prepared in conformity with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with the instructions to Form 10-Q and Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. Because the accompanying condensed consolidated financial statements do not include all of the information and footnotes required by GAAP, they should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2016 ("2016 Form 10-K"). In the opinion of management, all adjustments (consisting only of normal recurring accruals except as otherwise noted herein) considered necessary for a fair presentation of the results for the Company in the interim periods presented have been included. Results of operations for the three and six months ended June 30, 2017 are not necessarily indicative of the results that may be expected for the year ending December 31, 2017 or thereafter.

Walker & Dunlop, Inc. is a holding company and conducts the majority of its operations through Walker & Dunlop, LLC, the operating company. Walker & Dunlop is one of the leading commercial real estate services and finance companies in the United States. The Company originates, sells, and services a range of multifamily and other commercial real estate financing products and provides multifamily investment sales brokerage services. The Company originates and sells loans pursuant to the programs of the Federal National Mortgage Association ("Fannie Mae"), the Federal Home Loan Mortgage Corporation ("Freddie Mac," and together with Fannie Mae, the "GSEs"), the Government National Mortgage Association ("Ginnie Mae"), and the Federal Housing Administration, a division of the U.S. Department of Housing and Urban Development (together with Ginnie Mae, "HUD"). The Company also offers a proprietary loan program offering interim loans (the "Interim Program").

During the second quarter of 2017, the Company formed a joint venture with an affiliate of one of the world's largest owners of commercial real estate that originates, holds, and finances loans that previously met the criteria of the Interim Program. The Company holds a 15% ownership interest in the joint venture and is responsible for underwriting, servicing, and asset-managing the loans originated by the joint venture. The joint venture funds its operations using a combination of equity contributions from the partners and third-party credit facilities. The Company expects that substantially all loans satisfying the criteria for the Interim Program will be originated by the joint venture going forward; however, the Company may opportunistically originate loans held for investment through the existing Interim Program in the future. During the third quarter of 2017, the Company sold certain loans from its portfolio of interim loans with an unpaid principal balance of $119.8 million to the joint venture at par. These loans were classified as held for sale as of June 30, 2017. The Company does not expect to sell additional loans held for investment to the joint venture. The Company does not consolidate the activities of the joint venture; therefore, it accounts for the activities associated with its ownership interest using the equity method.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidation—The condensed consolidated financial statements include the accounts of Walker & Dunlop, Inc., its wholly owned subsidiaries, and its majority owned subsidiaries. All intercompany transactions have been eliminated in consolidation. When the Company has significant influence over operating and financial decisions for an entity but does not own a majority of the voting interests, the Company accounts for the investment using the equity method of accounting.

Subsequent Events—The Company has evaluated the effects of all events that have occurred subsequent to June 30, 2017. There have been no material events that would require recognition in the condensed consolidated financial statements. The Company has made certain disclosures in the notes to the condensed consolidated financial statements of events that have occurred subsequent to June 30, 2017. No other material subsequent events have occurred that would require disclosure.

Use of Estimates—The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses, including allowance for risk-sharing obligations, allowance for loan losses, capitalized mortgage servicing rights, derivative instruments, and the disclosure of contingent assets and liabilities. Actual results may vary from these estimates.

Comprehensive Income—For the three and six months ended June 30, 2017 and 2016, comprehensive income equaled net income; therefore, a separate statement of comprehensive income is not included in the accompanying condensed consolidated financial statements.

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Loans Held for Investment, net—Loans held for investment are multifamily loans originated by the Company through the Interim Program for properties that currently do not qualify for permanent GSE or HUD (collectively, the "Agencies") financing. These loans have terms of up to three years. The loans are carried at their unpaid principal balances, adjusted for net unamortized loan fees and costs, and net of any allowance for loan losses. Interest income is accrued based on the actual coupon rate, adjusted for the amortization of net deferred fees and costs, and is recognized as revenue when earned and deemed collectible. All loans held for investment are multifamily loans with similar risk characteristics. As of June 30, 2017, Loans held for investment, net consisted of nine loans with an aggregate $168.7 million of unpaid principal balance less $1.0 million of net unamortized deferred fees and costs and $0.2 million of allowance for loan losses. As of December 31, 2016, Loans held for investment, net consisted of 12 loans with an aggregate $222.3 million of unpaid principal balance less $1.5 million of net unamortized deferred fees and costs and $0.4 million of allowance for loan losses.

The allowance for loan losses is the Company's estimate of credit losses inherent in the interim loan portfolio at the balance sheet date. The Company has established a process to determine the appropriateness of the allowance for loan losses that assesses the losses inherent in the portfolio. That process includes assessing the credit quality of each of the loans held for investment by monitoring the financial condition of the borrower and the financial trends of the underlying property. The allowance levels are influenced by the outstanding portfolio balance, delinquency rates, historic loss experience, and other conditions influencing loss expectations, such as economic conditions. The allowance for loan losses is estimated collectively for loans with similar characteristics and for which there is no evidence of impairment. The allowances for loan losses recorded as of June 30, 2017 and December 31, 2016 were based on the Company's collective assessment of the portfolio.

Loans held for investment are placed on non-accrual status when full and timely collection of interest or principal is not probable. Loans held for investment are considered past due when contractually required principal or interest payments have not been made on the due dates and are charged off when the loan is considered uncollectible. The Company evaluates all loans held for investment for impairment. A loan is considered impaired when the Company believes that the facts and circumstances of the loan suggest that the Company will not be able to collect all contractually due principal and interest. Delinquency status and property financial condition are key components of the Company's consideration of impairment status.

None of the loans held for investment was delinquent, impaired, or on non-accrual status as of June 30, 2017 or December 31, 2016. Additionally, we have not experienced any delinquencies related to these loans or charged off any loan held for investment since the inception of the Interim Program in 2012.

Provision (Benefit) for Credit Losses—The Company records the income statement impact of the changes in the allowance for loan losses and the allowance for risk-sharing obligations within Provision (benefit) for credit losses in the Condensed Consolidated Statements of Income. NOTE 5 contains additional discussion related to the allowance for risk-sharing obligations. Provision (benefit) for credit losses consisted of the following activity for the three and six months ended June 30, 2017 and 2016:

(in thousands)	For the three months ended June 30, 2017	2016	For the six months ended June 30, 2017	2016
Provision (benefit) for loan losses	$ (215)	$ 17	$ (190)	$ (238)
Provision (benefit) for risk-sharing obligations	122			