

Edgar Filing: Waterstone Financial, Inc. - Form 10-Q

Waterstone Financial, Inc.  
Form 10-Q  
October 31, 2014  
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 September 30, 2014

OR

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number 001-36271  
WATERSTONE FINANCIAL, INC.

(Exact name of registrant as specified in its charter)

Maryland 90-1026709  
(State or other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

11200 W. Plank Court Wauwatosa, Wisconsin 53226  
(Address of principal executive offices) (Zip Code)

(414) 761-1000  
(Registrant's telephone number, including area code)

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 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, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if smaller reporting company)

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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 issuer's common stock, \$0.01 par value per share, was 34,420,094 at October 31, 2014

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WATERSTONE FINANCIAL, INC.

10-Q INDEX

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## PART I — FINANCIAL INFORMATION

Item 1. Financial StatementsWATERSTONE FINANCIAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

	(Unaudited)	
	September 30, 2014	December 31, 2013
	(In Thousands, except share data)	
Assets		
Cash	\$ 110,848	428,832
Federal funds sold	25,732	93
Interest-earning deposits in other financial institutions and other short term investments	4,702	244
Cash and cash equivalents	141,282	429,169
Securities available for sale (at fair value)	279,373	213,418
Loans held for sale (at fair value)	144,193	97,021
Loans receivable	1,111,719	1,092,676
Less: Allowance for loan losses	20,439	24,264
Loans receivable, net	1,091,280	1,068,412
Office properties and equipment, net	26,274	27,090
Federal Home Loan Bank stock (at cost)	17,500	17,500
Cash surrender value of life insurance	50,640	39,378
Real estate owned	25,837	22,663
Prepaid expenses and other assets	22,946	32,388
Total assets	\$ 1,799,325	1,947,039
Liabilities and Shareholders' Equity		
Liabilities:		
Demand deposits	\$ 90,600	93,275
Money market and savings deposits	119,974	513,716
Time deposits	664,577	637,750
Total deposits	875,151	1,244,741
Short-term borrowings	-	21,197
Long-term borrowings	434,000	434,000
Advance payments by borrowers for taxes	23,129	2,482
Other liabilities	18,532	30,147
Total liabilities	1,350,812	1,732,567
Shareholders' equity:		
Preferred stock (par value \$.01 per share)		
Authorized - 50,000,000 shares in 2014 and 20,000,000 in 2013, no shares issued	-	-
Common stock (par value \$.01 per share)		
Authorized - 100,000,000 shares in 2014 and 200,000,000 in 2013		
Issued - 34,420,094 in 2014 and 34,073,670 in 2013		
Outstanding - 34,420,094 in 2014 and 31,349,317 in 2013	344	341

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Additional paid-in capital	313,841	110,480
Retained earnings	156,611	151,195
Unearned ESOP shares	(22,848 )	(854 )
Accumulated other comprehensive income (loss), net of taxes	565	(1,429 )
Treasury shares (0 in 2014 and 2,724,353 in 2013), at cost	-	(45,261 )
Total shareholders' equity	448,513	214,472
Total liabilities and shareholders' equity	\$1,799,325	1,947,039

See Accompanying Notes to Unaudited Consolidated Financial Statements.

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WATERSTONE FINANCIAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF INCOME  
(Unaudited)

	Three months ended September 30, 2014		Nine months ended September 30, 2013	
	2014	2013	2014	2013
	(In Thousands, except per share amounts)			
Interest income:				
Loans	\$ 14,942	14,425	43,178	44,500
Mortgage-related securities	835	455	2,142	1,311
Debt securities, federal funds sold and short-term investments	823	653	2,474	1,806
Total interest income	16,600	15,533	47,794	47,617
Interest expense:				
Deposits	1,337	1,237	3,522	4,055
Borrowings	4,349	4,718	13,048	13,917
Total interest expense	5,686	5,955	16,570	17,972
Net interest income	10,914	9,578	31,224	29,645
Provision for loan losses	315	1,000	850	3,960
Net interest income after provision for loan losses	10,599	8,578	30,374	25,685
Noninterest income:				
Service charges on loans and deposits	317	316	904	1,029
Increase in cash surrender value of life insurance	630	528	1,082	929
Mortgage banking income	22,053	18,173	58,743	65,616
Loss on sale of available for sale securities	-	-	—	(9 )
Other	911	2,013	3,436	3,205
Total noninterest income	23,911	21,030	64,165	70,770
Noninterest expenses:				
Compensation, payroll taxes, and other employee benefits	18,169	16,575	51,418	53,001
Occupancy, office furniture, and equipment	2,577	2,218	7,883	5,995
Advertising	678	718	2,252	2,339
Data processing	582	516	1,701	1,476
Communications	430	398	1,250	1,148
Professional fees	441	626	1,471	1,762
Real estate owned	665	(163 )	1,918	(9 )
FDIC insurance premiums	336	516	1,046	1,569
Other	3,152	3,012	9,325	8,453
Total noninterest expenses	27,030	24,416	78,264	75,734
Income before income taxes	7,480	5,192	16,275	20,721
Income tax expense	2,715	1,973	5,857	7,950
Net income	\$ 4,765	3,219	10,418	12,771
Income per share:				
Basic	\$ 0.14	0.09	0.31	0.37
Diluted	\$ 0.14	0.09	0.31	0.37
Weighted average shares outstanding:				
Basic	33,003	34,196	33,759	34,174
Diluted	33,232	34,471	33,997	34,428

See Accompanying Notes to Unaudited Consolidated Financial Statements.

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WATERSTONE FINANCIAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(Unaudited)

	Three months ended September 30, 2014		2013		Nine months ended September 30, 2014		2013	
	(In Thousands)							
Net income	\$4,765	3,219	10,418	12,771				
Other comprehensive (loss) income, net of tax:								
Net unrealized holding (loss) gain on available for sale securities:								
Net unrealized holding (loss) gain arising during the period, net of tax benefit (expense) of \$116, (\$30), (\$1,281), \$2,090, respectively	(180 )	38	1,984	(3,184 )				
Reclassification adjustment for net loss (gain) included in net income during the period, net of tax (benefit) expense of \$0, \$0, (\$7), (\$4), respectively	-	-	10	5				
Total other comprehensive (loss) income	(180 )	38	1,994	(3,179 )				
Comprehensive income	\$4,585	3,257	12,412	9,592				

See Accompanying Notes to Unaudited Consolidated Financial Statements.



WATERSONE FINANCIAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY  
(Unaudited)

	Common Stock		Additional	Retained	Unearned	Accumulated	Treasury	Total
	Shares	Amount	Paid-In	Earnings	ESOP	Other	Shares	Shareholders'
	(In Thousands)		Capital		Shares	Comprehensive		Equity
						Income		
						(Loss)		
Balances at December 31, 2012	31,348	\$ 341	110,490	136,487	(1,708 )	2,285	(45,261 )	202,634
Comprehensive income:								
Net income	-	-	-	12,771	-	-	-	12,771
Other comprehensive loss	-	-	-	-	-	(3,179 )	-	(3,179 )
Total comprehensive income								9,592
ESOP shares committed to be released to Plan participants	-	-	(130 )	-	641	-	-	511
Stock based compensation	1	-	96	-	-	-	-	96
Balances at September 30, 2013	31,349	\$ 341	110,456	149,258	(1,067 )	(894 )	(45,261 )	212,833
Balances at December 31, 2013	31,349	\$ 341	110,480	151,195	(854 )	(1,429 )	(45,261 )	214,472
Comprehensive income:								
Net income	-	-	-	10,418	-	-	-	10,418
Other comprehensive income	-	-	-	-	-	1,994	-	1,994
Total comprehensive income								12,412
Purchase of ESOP Shares	-	-	-	-	(22,884 )	-	-	(22,884 )
ESOP shares committed to be released to Plan participants	-	-	5	-	890	-	-	895
Cash dividend, \$0.05 per share	-	-	-	(5,002 )	-	-	-	(5,002 )
Stock based compensation	14	-	198	-	-	-	-	198
Merger of Lamplighter Financial, MHC	(23,050)	(231 )	305	-	-	-	-	74

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Exchange of common stock	(8,299 )	(83 )	83	-	-	-	-	-
Treasury stock retired	-	(27 )	(45,234 )	-	-	-	45,261	-
Proceeds of stock offering, net of costs	34,406	344	248,004	-	-	-	-	248,348
Balances at September 30, 2014	34,420	\$ 344	313,841	156,611	(22,848 )	565	-	448,513

See Accompanying Notes to Unaudited Consolidated Financial Statements.

WATERSTONE FINANCIAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)

	Nine months ended September 30, 2014            2013 (In Thousands)	
Operating activities:		
Net income	\$ 10,418	12,771
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Provision for loan losses	850	3,960
Provision for depreciation	2,463	1,936
Deferred income taxes	1,897	4,586
Stock based compensation	149	96
Net amortization of premium/discount on debt and mortgage related securities	1,215	1,764
Amortization of unearned ESOP shares	895	511
Amortization and impairment of mortgage servicing rights	321	790
Gain on sale of loans held for sale	(52,764 )	(56,776 )
Loans originated for sale	(1,256,795)	(1,419,834)
Proceeds on sales of loans originated for sale	1,262,387	1,513,039
Increase in accrued interest receivable	(420 )	(499 )
Increase in cash surrender value of life insurance	(1,082 )	(929 )
Decrease in accrued interest on deposits and borrowings	(46 )	(142 )
Increase (decrease) in other liabilities	552	(4,590 )
Increase (decrease) in accrued tax payable	1,692	(2,980 )
Loss on sale of available for sale securities	-	9
Net loss (gain) related to real estate owned	591	(1,313 )
Gain on sale of mortgage servicing rights	(2,393 )	(1,345 )
Other	7,191	(3,722 )
Net cash (used in) provided by operating activities	(22,879 )	47,332
Investing activities:		
Net (increase) decrease in loans receivable	(37,141 )	21,084
Purchases of:		
Debt securities	(15,997 )	(37,595 )
Mortgage related securities	(80,837 )	(11,182 )
Certificates of deposit	(735 )	(1,225 )
Premises and equipment, net	(1,703 )	(3,768 )
Bank owned life insurance	(10,180 )	(241 )
Proceeds from:		
Principal repayments on mortgage-related securities	20,662	30,505
Maturities of debt securities	13,020	4,925
Sales of debt securities	-	921
Sales of real estate owned	9,579	23,312
Net cash (used in) provided by investing activities	(103,332 )	26,736
Financing activities:		
Net increase (decrease) in deposits	20,714	(67,228 )

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Net decrease in short-term borrowings	(21,197 )	(8,645 )
Net change in advance payments by borrowers for taxes	6,911	8,243
Cash dividends on common stock	(3,387 )	-
Financing for purchase of ESOP	(22,884 )	-
Proceeds from stock option exercises	49	-
Stock offering funds returned to subscribers	(141,882 )	-
Net cash used in financing activities	(161,676 )	(67,630 )
(Decrease) increase in cash and cash equivalents	(287,887 )	6,438
Cash and cash equivalents at beginning of period	429,169	71,469
Cash and cash equivalents at end of period	\$ 141,282	77,907

Supplemental information:

Cash paid or credited during the period for:

Income tax payments	2,199	6,263
Interest payments	16,616	18,114
Noncash activities:		
Loans receivable transferred to real estate owned	13,423	10,117
Deposits utilized to purchase common stock	248,422	-
Dividends declared but not paid in other liabilities	1,615	-

See Accompanying Notes to Unaudited Consolidated Financial Statements.

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WATERSTONE FINANCIAL, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

Note 1 — Basis of Presentation

On June 6, 2013, the Board of Directors of Lamplighter Financial, MHC ("MHC") and the Board of Directors of Waterstone Financial, Inc., a federal corporation, ("Waterstone-Federal") adopted a Plan of Conversion and Reorganization (the "Plan"). Pursuant to the Plan, Waterstone Financial, Inc., a Maryland corporation, ("New Waterstone") was organized and the MHC converted from the mutual holding company form of organization to the fully public form on January 22, 2014. As part of the conversion, the MHC's ownership interest of Waterstone-Federal was offered for sale in a public offering. A total of 25,300,000 shares were sold in the offering at a price \$10.00 per share, resulting in gross proceeds of \$253.0 million. Expenses related to the offering totaled approximately \$4.7 million. The existing publicly held shares of Waterstone-Federal were exchanged for new shares of common stock of New Waterstone at a conversion ratio of 1.0973-to-one. The exchange ratio ensured that immediately after the conversion and public offering, the public shareholders of Waterstone-Federal owned the same aggregate percentage of New Waterstone common stock that they owned immediately prior to that time (excluding shares purchased in the stock offering and cash received in lieu of fractional shares). When the conversion and public offering was completed, New Waterstone became the holding company of WaterStone Bank SSB and succeeded to all of the business and operations of Waterstone-Federal and each of Waterstone-Federal and Lamplighter Financial, MHC ceased to exist. Approximately 34,405,458 shares of New Waterstone common stock were outstanding after the completion of the offering and exchange.

The Plan provided for the establishment of special "liquidation accounts" for the benefit of certain depositors of WaterStone Bank in an amount equal to the greater of the MHC's ownership interest in the retained earnings of the Company as of the date of the latest balance sheet contained in the prospectus or the retained earnings of WaterStone Bank at the time it reorganized into the MHC. Following the completion of the conversion, under the rules of the Board of Governors of the Federal Reserve System, WaterStone Bank is not permitted to pay dividends on its capital stock to Waterstone Financial, Inc., its sole shareholder, if WaterStone Bank's shareholder's equity would be reduced below the amount of the liquidation accounts. The liquidation accounts will be reduced annually to the extent that eligible account holders have reduced their qualifying deposits. Subsequent increases will not restore an eligible account holder's interest in the liquidation accounts.

Share and per share amounts have been restated to reflect the completion of our second-step conversion on January 22, 2014 at a conversion ratio of 1.0973 unless noted otherwise.

The unaudited interim consolidated financial statements include the accounts of Waterstone Financial, Inc. (the "Company") and the Company's subsidiaries.

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles ("GAAP") for interim financial information, Rule 10-01 of Regulation S-X and the instructions to Form 10-Q. The financial statements do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments (consisting of normal recurring accruals) necessary to present fairly the financial position, results of operations, changes in shareholders' equity, and cash flows of the Company for the periods presented.

The accompanying unaudited consolidated financial statements and related notes should be read in conjunction with the Company's December 31, 2013 Annual Report on Form 10-K. Operating results for the three and nine months ended September 30, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014 or for any other period.

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The preparation of the unaudited consolidated financial statements requires management of the Company to make a number of estimates and assumptions relating to the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the period. Significant items subject to such estimates and assumptions include the allowance for loan losses, deferred income taxes and real estate owned. Actual results could differ from those estimates.

Certain prior period amounts have been reclassified to conform to current period presentation. These reclassifications did not result in any changes to previously reported net income or shareholders' equity.

### Impact of Recent Accounting Pronouncements

In July 2013, th