

LUMINENT MORTGAGE CAPITAL INC

Form 10-Q

December 27, 2007

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 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 September 30, 2007

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: 000-31828**

LUMINENT MORTGAGE CAPITAL, INC.
(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of
incorporation or organization)

06-1694835
(I.R.S. Employer
Identification No.)

**101 California Street, Suite 1350, San Francisco,
California**

94111
(Zip Code)

(Address of principal executive offices)

(415) 217-4500

(Registrant's telephone number, including area code)

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

Indicate by check mark whether 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 registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" as defined in Rule 12b-2 of the Exchange Act. (Check one)

Large accelerated filer 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 .

The number of shares of common stock outstanding on December 24, 2007 was 43,172,839.

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Form 10-Q contains or incorporates by reference certain forward-looking statements under the Private Securities Litigation Reform Act of 1995. Forward-looking statements convey our current expectations or forecasts of future events. All statements contained in this Form 10-Q other than statements of historical fact are forward-looking statements. Words such as anticipates, estimates, expects, projects, intends, plans, believes and words and similar substance used in connection with any discussion of future operating or financial performance identify forward-looking statements.

We claim the protection of the safe harbor for forward-looking statements provided in the Private Securities Litigation Reform Act of 1995. These statements may be made directly in this Form 10-Q and they may also be incorporated by reference in this Form 10-Q to other documents we file with the SEC. We base our forward-looking statements upon the current beliefs and expectations of our management and they are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are difficult to predict and generally beyond our control. In addition, these forward-looking statements are subject to assumptions with respect to future business strategies and decisions that are subject to change. Actual results may differ materially from the anticipated results discussed in these forward-looking statements. These forward-looking statements include, among other things, statements about:

- our ability to meet margin calls on our repurchase agreement financing that may be required due to further declines in the value of the mortgage-backed securities collateralizing the agreements;
- our ability to obtain or renew sufficient funding to maintain our leverage strategies and support our liquidity position;
- the continued creditworthiness of the holders of mortgages underlying our mortgage-related assets;
- our ability to purchase sufficient mortgages for our securitization business;
- the effect of the flattening of, or other changes in, the yield curve on our investment strategies;
- changes in interest rates and mortgage prepayment rates;
- the possible effect of negative amortization of mortgages on our financial condition and REIT qualification;
- the possible impact of our failure to regain or maintain exemptions under the 1940 Act;
- potential impacts of our leveraging policies on our net income and cash available for distribution;
- the power of our board of directors to change our operating policies and strategies without stockholder approval;
- the effects of interest rate caps and or proposed federal legislation on our adjustable-rate and hybrid adjustable-rate loans and mortgage-backed securities;
- the degree to which our hedging strategies may or may not protect us from interest rate volatility;
- our ability to invest up to 10% of our investment portfolio in residuals, leveraged mortgage derivative securities and shares of other REITs as well as other investments;
- our current inability to make cash distributions to our stockholders because of our liquidity concerns; and

the other factors described in this Form 10-Q, including those under the captions Management's Discussion and Analysis of Financial Condition and Results of Operations, Risk Factors and Quantitative and Qualitative Disclosures about Market Risk.

We caution you not to place undue reliance on these forward-looking statements, which speak only as of the date of this Form 10-Q or the date of any document incorporated by reference in this Form 10-Q. All subsequent written and oral forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. Except to the extent required by applicable law or regulation, we undertake no obligation to update these forward-looking statements to reflect events or circumstances after the date of this Form 10-Q or to reflect the occurrence of unanticipated events.

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PART I
FINANCIAL INFORMATION

Item 1. Financial Statements.

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**LUMINENT MORTGAGE CAPITAL, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS**

	September 30, 2007 (Unaudited)	December 31, 2006
(in thousands, except share and per share amounts)		
Assets:		
Cash and cash equivalents	\$ 8,285	\$ 5,902
Restricted cash	8,396	7,498
Loans held-for-investment, net of allowance for loan losses of \$21,282 at September 30, 2007 and \$5,020 at December 31, 2006	4,369,019	5,591,717
Mortgage-backed securities, at fair value		141,556
Mortgage-backed securities pledged as collateral, at fair value	907,005	2,789,382
Debt securities, at fair value	1,006	
Equity securities, at fair value	413	1,098
Interest receivable	24,023	36,736
Principal receivable	1,771	1,029
Derivatives, at fair value	201	13,021
Other assets	52,318	25,856
Total assets	\$ 5,372,437	\$ 8,613,795
Liabilities:		
Mortgage-backed notes	\$ 4,030,643	\$ 3,917,677
Repurchase agreements	792,231	2,707,915
Warehouse lending facilities		752,777
Commercial paper		637,677
Collateralized debt obligations	294,529	
Junior subordinated notes	92,788	92,788
Convertible senior notes	90,000	
Derivatives, at fair value	2,623	
Revolving line of credit	43,256	
Cash distributions payable	13,857	14,343
Accrued interest expense	14,231	12,094
Warrant liability, at fair value	68,910	
Accounts payable and accrued expenses	19,854	6,969
Total liabilities	5,462,922	8,142,240
Stockholders Equity:		
Preferred stock, par value \$0.001:		
10,000,000 shares authorized; no shares issued and outstanding at September 30, 2007 and December 31, 2006		
Common stock, par value \$0.001:		

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100,000,000 shares authorized; 43,172,839 and 47,808,510 shares issued and outstanding at September 30, 2007 and December 31, 2006, respectively	43	48
Additional paid-in capital	548,459	583,492
Accumulated other comprehensive income	2,560	3,842
Accumulated distributions in excess of accumulated earnings	(641,547)	(115,827)
Total stockholders' equity (deficit)	(90,485)	471,555
Total liabilities and stockholders' equity (deficit)	\$ 5,372,437	\$ 8,613,795

See notes to condensed consolidated financial statements

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LUMINENT MORTGAGE CAPITAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

(in thousands, except share and per share amounts)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2007	2006	2007	2006
Net interest income:				
Interest income:				
Mortgage loan and securitization portfolio	\$ 86,869	\$ 65,658	\$ 281,527	\$ 133,667
Spread portfolio	21,850	18,947	84,001	69,757
Credit sensitive bond portfolio	25,268	10,493	60,495	28,176
Total interest income	133,987	95,098	426,023	231,600
Interest expense	112,392	73,149	349,819	172,633
Net interest income	21,595	21,949	76,204	58,967
Other income (expenses):				
Gains (losses) on derivative instruments, net	6,524	(11,689)	42,406	4,087
Gains (losses) on sales of mortgage-backed securities, net	(137,959)	167	(153,409)	990
Losses on sales of loans held-for-investment	(46,477)		(46,477)	
Impairment losses on mortgage-backed securities	(268,877)		(287,622)	(2,179)
Mortgage-backed securities, trading change in fair value	(18,209)		(18,200)	
Warrants, change in fair value	(46,569)		(46,569)	
Other expense	(49)		(156)	(608)
Total other income (expenses)	(511,616)	(11,522)	(510,027)	2,290
Operating Expenses:				
Servicing expense	5,389	3,526	18,104	7,546
Provision for loan losses	10,247	1,779	18,434	3,304
Salaries and benefits	8,363	2,934	14,998	7,375
Professional services	3,171	1,088	5,012	2,181
Management compensation expense to related party		6,048		7,712
Other general and administrative expenses	1,690	1,242	5,366	3,334
Total operating expenses	28,860	16,617	61,914	31,452
Income (loss) before income taxes	(518,881)	(6,190)	(495,737)	29,805

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Income taxes		1,755	405	1,709	1,057
Net income (loss)		\$ (520,636)	\$ (6,595)	\$ (497,446)	\$ 28,748
Net income (loss) per share	basic	\$ (12.17)	\$ (0.17)	\$ (11.07)	\$ 0.74
Net income (loss) per share	diluted	\$ (12.17)	\$ (0.17)	\$ (11.07)	\$ 0.74
Weighted-average number of shares outstanding	basic	42,790,740	38,695,800	44,943,803	38,937,454
Weighted-average number of shares outstanding	diluted	42,790,740	38,695,800	44,943,803	39,066,406
Dividends per share		\$	\$ 0.30	\$ 0.62	\$ 0.55

See notes to condensed consolidated financial statements

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LUMINENT MORTGAGE CAPITAL, INC.
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY (DEFICIT)
(Unaudited)

(in thousands)	Common Stock Shares	Par Value	Additional Paid-in Capital	Other Comprehensive Income/(Loss)	Accumulated Distributions in Excess of Accumulated Earnings	Comprehensive Income/(Loss)	Total
Balance, January 1, 2007	47,809	\$ 48	\$ 583,492	\$ 3,842	\$ (115,827)		\$ 471,555
Net income (loss)					(497,446)	\$ (497,446)	(497,446)
Securities available-for-sale, fair value adjustment				(105)		(105)	(105)
Amortization of derivative gains				(1,177)		(1,177)	(1,177)
Comprehensive income (loss)						\$ (498,728)	
Repurchases and retirement of common stock	(4,905)	(5)	(41,290)				(41,295)
Distributions to stockholders					(28,274)		(28,274)
Issuance and amortization of restricted common stock	269		6,257				6,257
Balance, September 30, 2007	43,173	\$ 43	\$ 548,459	\$ 2,560	\$ (641,547)		\$ (90,485)

See notes to condensed consolidated financial statements

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LUMINENT MORTGAGE CAPITAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(in thousands)	For the Nine Months Ended September 30,	
	2007	2006
Cash flows from operating activities:		
Net income (loss)	\$ (497,446)	\$ 28,748
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Amortization of premium/(discount) on loans held-for-investment and mortgage-backed securities and depreciation	20,652	(941)
Impairment losses on securities	287,622	2,179
Provision for loan losses	18,434	3,304
Realized loss on real estate owned	491	
Negative amortization of loans held-for-investment	(86,531)	(35,004)
Share-based compensation	6,257	2,594
Net realized and unrealized (gains) losses on derivative instruments	7,156	(3,459)
Net losses on mortgage backed securities held as trading	18,200	
Net change in the fair value of warrants	46,569	
Net (gain) losses on sales of mortgage-backed-securities available-for-sale	153,409	(990)
Net losses on the sales of loans held-for-investment	46,477	
Changes in operating assets and liabilities:		
(Increase) decrease in interest receivable, net of purchased interest	(16,048)	73
(Increase) decrease in other assets	2,452	(2,042)
Increase in accounts payable and other liabilities	12,304	890
Increase (decrease) in accrued interest expense	2,742	(13,183)
Increase in management compensation payable, incentive compensation payable and other related-party payable		4,949
Net cash provided by (used in) operating activities	22,740	(12,882)
Cash flows from investing activities:		
Purchases of mortgage-backed securities	(821,436)	(1,849,595)
Proceeds from sales of mortgage-backed securities	1,863,969	3,750,554
Principal payments of mortgage-backed securities	376,188	364,781
Purchases of loans held-for-investment, net	(1,679,991)	(3,949,480)
Principal payments of loans held-for-investment	1,295,362	272,476
Proceeds from the sale of loans held-for-investment	957,150	
Purchases of derivative instruments	(32,979)	(2,792)
Proceeds from derivative instruments	40,184	3,484
Purchase of debt securities	(1,271)	
Net change in restricted cash	(8,437)	671
Other	(129)	
Net cash provided by (used in) investing activities	1,988,610	(1,409,901)

Cash flows from financing activities:

Proceeds from issuance of common stock		11,747
Repurchases of common stock	(41,295)	(15,832)
Capitalized financing costs	(2,355)	
Borrowings under repurchase agreements	31,313,807	27,681,403
Principal payments on repurchase agreements	(33,021,207)	(29,080,973)
Borrowings under warehouse lending facilities	2,069,957	3,806,251
Paydown of warehouse lending facilities	(2,822,551)	(3,806,251)
Borrowings under commercial paper facility	3,849,451	
Paydown of commercial paper facility	(4,487,127)	
Distributions to stockholders	(28,760)	(11,014)
Proceeds from issuance of mortgage-backed notes	1,763,061	3,062,397
Principal payments on mortgage-backed notes	(1,025,663)	(214,187)
Proceeds from issuance of collateralized debt obligations	291,027	
Principal payments on collateralized debt obligations	(568)	
Principal payments on margin debt		(3,548)
Proceeds from issuance of convertible senior notes	90,000	
Proceeds from revolving line of credit	43,256	
Net cash provided by (used in) financing activities	(2,008,967)	1,429,993
Net increase in cash and cash equivalents	2,383	7,210
Cash and cash equivalents, beginning of the period	5,902	11,466