

RADIAN GROUP INC
Form 10-Q
November 10, 2008
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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 September 30, 2008

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 1-11356

Radian Group Inc.

(Exact name of registrant as specified in its charter)

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Delaware (State or other jurisdiction of incorporation or organization)	23-2691170 (I.R.S. Employer Identification No.)
1601 Market Street, Philadelphia, PA (Address of principal executive offices)	19103 (Zip Code)
(215) 231-1000 (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 is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check One):

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 81,124,288 shares of common stock, \$0.001 par value per share, outstanding on November 3, 2008.

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Forward Looking Statements Safe Harbor Provisions

All statements in this report that address events, developments or results that we expect or anticipate may occur in the future are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, Section 21E of the Securities Exchange Act of 1934 and the U.S. Private Securities Litigation Reform Act of 1995. In most cases, forward-looking statements may be identified by words such as anticipate, may, should, expect, intend, plan, goal, contemplate, believe, estimate, predict, project, potential, continue or the negative or words and other similar expressions. These statements, which include, without limitation, projections regarding our future performance and financial condition are made on the basis of management's current views and assumptions with respect to future events. Any forward-looking statement is not a guarantee of future performance and actual results could differ materially from those contained in the forward-looking information. The forward-looking statements, as well as our prospects as a whole, are subject to risks and uncertainties, including the following:

changes in general financial and political conditions, such as extended national or regional economic recessions, changes in housing demand or mortgage originations, changes in housing values (in particular, further deterioration in the housing, mortgage and related credit markets, which would harm our future consolidated results of operations and could cause losses for our businesses to be worse than expected), changes in the liquidity in the capital markets and the further contraction of credit markets, population trends and changes in household formation patterns, changes in unemployment rates, changes or volatility in interest rates or consumer confidence, changes in credit spreads, changes in the way investors perceive the strength of private mortgage insurers or financial guaranty providers, investor concern over the credit quality and specific risks faced by the particular businesses, municipalities or pools of assets covered by our insurance;

economic changes or catastrophic events in geographic regions where our mortgage insurance or financial guaranty insurance in force is more concentrated;

our ability to successfully execute upon our capital plan, and if necessary, to obtain additional capital, to support our long-term liquidity needs and to protect our credit ratings and the financial strength ratings of Radian Guaranty Inc., our primary mortgage insurance subsidiary;

a further decrease in the volume of home mortgage originations due to reduced liquidity in the lending market, tighter underwriting standards and the on-going deterioration in housing markets throughout the U.S.;

our ability to maintain adequate risk-to-capital ratios, leverage ratios and surplus requirements in our mortgage insurance business in light of on-going losses in this business;

the concentration of our mortgage insurance business among a relatively small number of large customers;

disruption in the servicing of mortgages covered by our insurance policies;

the aging of our mortgage insurance portfolio and changes in severity or frequency of losses associated with certain of our products that are riskier than traditional mortgage insurance or financial guaranty insurance policies;

the performance of our insured portfolio of higher risk loans, such as Alternative-A (Alt-A) and subprime loans, and adjustable rate products, such as adjustable rate mortgages and interest-only mortgages, which have resulted in increased losses in 2007 and 2008 and are expected to result in further losses;

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reduced opportunities for loss mitigation in markets where housing values fail to appreciate or begin to decline;

changes in persistency rates of our mortgage insurance policies caused by changes in refinancing activity, in the rate of appreciation or depreciation of home values and changes in the mortgage insurance cancellation requirements of mortgage lenders and investors;

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downgrades or threatened downgrades of, or other ratings actions with respect to, our credit ratings or the ratings assigned by the major rating agencies to any of our rated insurance subsidiaries at any time (in particular, the credit rating of Radian Group Inc. and the financial strength ratings assigned to Radian Guaranty Inc., which are currently on Negative outlook); which risk is discussed in more detail below in Item 2 of Part I of this report on Form 10-Q;

heightened competition for our mortgage insurance business from others such as the Federal Housing Administration and the Veterans Administration or other private mortgage insurers (in particular those that have been assigned higher ratings from the major rating agencies);

changes in the charters or business practices of Federal National Mortgage Association (Fannie Mae) and Freddie Mac, the largest purchasers of mortgage loans that we insure, and our ability to retain our Top Tier eligibility requirement from both Freddie Mac and Fannie Mae;

the application of existing federal or state consumer, lending, insurance, securities and other applicable laws and regulations, or changes in these laws and regulations or the way they are interpreted; including, without limitation: (i) the outcome of existing investigations or the possibility of private lawsuits or other formal investigations by state insurance departments and state attorneys general alleging that services offered by the mortgage insurance industry, such as captive reinsurance, pool insurance and contract underwriting, are violative of the Real Estate Settlement Procedures Act and/or similar state regulations, (ii) legislative and regulatory changes affecting demand for private mortgage insurance or financial guaranty insurance, or (iii) legislation and regulatory changes limiting or restricting our use of (or requirements for) additional capital, the products we may offer, the form in which we may execute the credit protection we provide or the aggregate notional amount of any product we may offer for any one transaction or in the aggregate;

the possibility that we may fail to estimate accurately the likelihood, magnitude and timing of losses in connection with establishing loss reserves for our mortgage insurance or financial guaranty businesses, or the premium deficiencies for our first- and second-lien mortgage insurance business, or to estimate accurately the fair value amounts of derivative contracts in our mortgage insurance and financial guaranty businesses in determining gains and losses on these contracts;

volatility in our earnings caused by changes in the fair value of our derivative instruments and our need to reevaluate the premium deficiencies in our mortgage insurance business on a quarterly basis;

changes in accounting guidance from the Securities and Exchange Commission (SEC) or the Financial Accounting Standards Board;

legal and other limitations on amounts we may receive from our subsidiaries as dividends or through tax and expense sharing arrangements with our subsidiaries; and

vulnerability to the performance of our investment in Sherman Financial Group LLC.

For more information regarding these risks and uncertainties as well as certain additional risks that we face, you should refer to the Risk Factors detailed in Item 1A of Part I of our Annual Report on Form 10-K for the year ended December 31, 2007 as well as the material changes to these risks discussed in Item 1A of Part II of our quarterly reports on Form 10Q, including the material changes discussed in this report below. We caution you not to place undue reliance on these forward-looking statements, which are current only as of the date on which we filed this report. We do not intend to, and we disclaim any duty or obligation to, update or revise any forward-looking statements made in this report to reflect new information or future events or for any other reason.

Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements.****Radian Group Inc.****CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)**

(\$ in thousands, except per-share amounts)	September 30 2008	December 31 2007
ASSETS		
Investments		
Fixed maturities held to maturity at amortized cost (fair value \$37,605 and \$55,021)	\$ 36,648	\$ 53,310
Fixed maturities available for sale at fair value (amortized cost \$4,379,209 and \$4,571,998)	4,177,994	4,644,724
Trading securities at fair value (amortized cost \$538,109 and \$158,087)	521,641	153,634
Equity securities available for sale at fair value (cost \$215,040 and \$196,068)	208,158	254,869
Hybrid securities at fair value (amortized cost \$552,087 and \$525,607)	493,281	584,373
Short-term investments	764,285	697,271
Other invested assets (cost \$20,617 and \$21,087)	21,245	22,868
Total investments	6,223,252	6,411,049
Cash	106,962	200,787
Investment in affiliates	87,256	104,354
Deferred policy acquisition costs	178,581	234,955
Prepaid federal income taxes	248,828	793,486
Accrued investment income	71,070	65,362
Accounts and notes receivable (less allowance of \$59,545 and \$50,391)	93,127	130,773
Property and equipment, at cost (less accumulated depreciation of \$87,560 and \$81,930)	22,275	24,567
Derivative assets	171,116	43,214
Tax recoverables	270,775	1,816
Reinsurance recoverables	310,984	33,960
Other assets	262,010	165,866
Total assets	\$ 8,046,236	\$ 8,210,189
LIABILITIES AND STOCKHOLDERS' EQUITY		
Unearned premiums	\$ 1,000,725	\$ 1,094,710
Reserve for losses and loss adjustment expenses	2,680,381	1,598,756
Reserve for premium deficiency	331,373	195,646
Long-term debt and other borrowings	908,282	953,524
Variable interest entity debt	127,624	
Deferred income taxes payable		26,705
Derivative liabilities	343,296	1,305,665
Accounts payable and accrued expenses	322,229	314,447
Total liabilities	5,713,910	5,489,453
Commitments and Contingencies (Note 15)		
Stockholders' equity		
Common stock: par value \$.001 per share; 325,000,000 and 200,000,000 shares authorized at September 30, 2008 and December 31, 2007; 97,792,163 and 97,631,763 shares issued at September 30, 2008 and December 31, 2007; 80,696,131 and 80,412,974 shares outstanding at September 30, 2008 and December 31, 2007, respectively	98	98

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Treasury stock, at cost: 17,096,032 and 17,218,789 shares at September 30, 2008 and December 31, 2007, respectively	(883,796)	(889,478)
Additional paid-in capital	1,337,632	1,331,790
Retained earnings	2,017,542	2,181,191
Accumulated other comprehensive income	(139,150)	97,135
 Total stockholders' equity	 2,332,326	 2,720,736
 Total liabilities and stockholders' equity	 \$ 8,046,236	 \$ 8,210,189

See notes to unaudited condensed consolidated financial statements.

Table of Contents**Radian Group Inc.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)**

(In thousands, except per-share amounts)	Three Months Ended September 30		Nine Months Ended September 30	
	2008	2007	2008	2007
Revenues:				
Premiums written insurance:				
Direct	\$ 232,656	\$ 307,797	\$ 743,922	\$ 820,409
Assumed	8,507	37,209	45,820	89,805
Ceded	(38,712)	(36,995)	(120,340)	(111,354)
Net premiums written	202,451	308,011	669,402	798,860
Decrease (increase) in unearned premiums	47,267	(62,615)	71,374	(120,947)
Net premiums earned insurance	249,718	245,396	740,776	677,913
Net investment income	65,215	64,959	196,322	188,605
Change in fair value of derivative instruments	164,757	(615,936)	928,792	(633,765)
Net (losses) gains on other financial instruments	(63,737)	14,840	(126,872)	54,279
Gain on sale of affiliate		181,734		181,734
Other income	2,756	4,599	9,591	11,519
Total revenues	418,709	(104,408)	1,748,609	480,285
Expenses:				
Provision for losses	544,915	330,504	1,586,505	611,508
Provision for premium deficiency	(252,170)	155,176	135,727	155,176
Policy acquisition costs	20,770	35,743	120,628	88,195
Other operating expenses	80,781	36,169	199,771	151,472
Interest expense	13,852	13,394	40,177	38,810
Total expenses	408,148	570,986	2,082,808	1,045,161
Equity in net income (loss) of affiliates	15,798	(448,924)	44,028	(376,645)
Pretax (loss) income	26,359	(1,124,318)	(290,171)	(941,521)
Income tax benefit	(10,340)	(420,454)	(129,984)	(372,207)
Net (loss) income	\$ 36,699	\$ (703,864)	\$ (160,187)	\$ (569,314)
Basic net (loss) income per share	\$ 0.46	\$ (8.82)	\$ (2.01)	\$ (7.16)
Diluted net (loss) income per share	\$ 0.46	\$ (8.82)	\$ (2.01)	\$ (7.16)
Weighted average number of common shares outstanding basic	79,960	79,800	79,603	79,467
Weighted average number of common and common equivalent shares outstanding diluted	80,471	79,800	79,603	79,467
Dividends per share	\$ 0.0025	\$ 0.02	\$ 0.0425	\$ 0.06

See notes to unaudited condensed consolidated financial statements.

Table of Contents**Radian Group Inc.****CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN COMMON STOCKHOLDERS EQUITY (UNAUDITED)**

(In thousands)	Common Stock		Treasury Stock	Additional Paid-in Capital	Retained Earnings	Foreign Currency Translation Adjustment	Accumulated Other Comprehensive Income (Loss)		Total
	Stock	Stock					Unrealized Gains (Losses)	Other	
BALANCE prior to implementation effects JANUARY 1, 2007	\$ 97	\$ (931,012)	\$ 1,347,205	\$ 3,489,290	\$ 9,796	\$ 151,934	\$ 247	\$ 4,067,557	
Cumulative effect of adoption of FIN No. 48				(21,214)				(21,214)	
Cumulative effect of adoption of SFAS No. 155				9,844			(9,844)		
BALANCE, JANUARY 1, 2007, as adjusted	97	(931,012)	1,347,205	3,477,920	9,796	142,090	247	4,046,343	
Comprehensive loss:									
Net loss				(569,314)				(569,314)	
Unrealized foreign currency translation adjustment, net of tax of \$4,446					8,256			8,256	
Unrealized holding losses arising during period, net of tax benefit of \$24,743							(45,951)		
Less: Reclassification adjustment for net gains included in net income, net of tax of \$4,129							(7,669)		
Net unrealized loss on investments, net of tax benefit of \$28,872							(53,620)	(53,620)	
Comprehensive loss								(614,678)	
Issuance of common stock under incentive plans		64,727	5,943					70,670	
Issuance of restricted stock			(34,662)					(34,662)	
Amortization of restricted stock			6,341					6,341	
Stock-based compensation expense-options			1,109					1,109	
Treasury stock purchased		(22,823)						(22,823)	
Dividends paid				(4,808)				(4,808)	
BALANCE, SEPTEMBER 30, 2007	\$ 97	\$ (889,108)	\$ 1,325,936	\$ 2,903,798	\$ 18,052	\$ 88,470	\$ 247	\$ 3,447,492	
BALANCE, JANUARY 1, 2008,	\$ 98	\$ (889,478)	\$ 1,331,790	\$ 2,181,191	\$ 12,142	\$ 86,619	\$ (1,626)	\$ 2,720,736	
Comprehensive loss:									
Net loss				(160,187)				(160,187)	
Unrealized foreign currency translation adjustment, net of tax of \$29					(54)			(54)	
Unrealized holding losses arising during the period, net of tax benefit of \$132,949							(246,905)		
Less: Reclassification adjustment for net losses included in net loss, net of tax benefit of \$13,758							25,551		
Net unrealized loss on investments, net of tax benefit of \$119,191							(221,354)	(221,354)	
Comprehensive loss								(381,595)	
Sherman equity adjustment							(16,761)	(16,761)	
Pension curtailment							1,884	1,884	
Repurchases of common stock under incentive plans		5,682	(5,992)					(310)	
Issuance of restricted stock			476					476	
Amortization of restricted stock			6,297					6,297	
Stock-based compensation expense			5,061					5,061	
Dividends declared				(3,462)				(3,462)	

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BALANCE, SEPTEMBER 30, 2008 \$ 98 \$ (883,796) \$ 1,337,632 \$ 2,017,542 \$ 12,088 \$ (134,735) \$ (16,503) \$ 2,332,326

See notes to unaudited condensed consolidated financial statements.

Table of Contents**Radian Group Inc.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)**

(In thousands)	Nine Months Ended September 30	
	2008	2007
Cash flows (used in) provided by operating activities	\$ (123,957)	\$ 324,058
Cash flows from investing activities:		
Proceeds from sales of fixed-maturity investments available for sale	547,718	210,850
Proceeds from sales of equity securities available for sale	93,896	44,352
Proceeds from sales of hybrid securities	264,690	261,156
Proceeds from redemptions of fixed-maturity investments available for sale	150,161	168,294
Proceeds from redemptions of fixed-maturity investments held to maturity	17,953	20,841
Proceeds from redemptions of hybrid securities	29,347	52,971
Purchases of fixed-maturity investments available for sale	(519,936)	(513,374)
Purchases of equity securities available for sale	(114,933)	(6,822)
Purchases of hybrid securities	(318,151)	(334,437)
Sales (purchases) of short-term investments, net	(73,854)	(639,360)
Purchases of other invested assets, net	(1,921)	(7,278)
Purchases of property and equipment, net	(3,991)	(2,728)
Sale (purchase) of investment in affiliates		277,882
Loan to affiliate		(50,000)
Net cash provided by (used) in investing activities	70,979	(517,653)
Cash flows from financing activities:		
Dividends paid	(3,462)	(4,808)
Proceeds from issuance of common stock under incentive plans		25,281
Proceeds from (paydown of) other borrowings	(50,000)	200,000
Excess tax benefits from stock-based awards		5,488
Purchase of treasury stock		(22,823)
Proceeds from termination of interest-rate swap	12,800	
Net cash (used in) provided by financing activities	(40,662)	203,138
Effect of exchange rate changes on cash	(185)	(4,644)
(Decrease) increase in cash	(93,825)	4,899
Cash, beginning of period	200,787	57,901
Cash, end of period	\$ 106,962	\$ 62,800
Supplemental disclosures of cash flow information:		
Income taxes (received) paid	\$ (508,756)	\$ 128,308
Interest paid	\$ 38,368	\$ 33,741
Supplemental disclosures of non-cash items:		
Stock-based compensation, net of tax	\$ 10,914	\$ 1,939

See notes to unaudited condensed consolidated financial statements.