

WESTWOOD HOLDINGS GROUP INC
Form 10-Q
July 23, 2008

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 June 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 1-31234

WESTWOOD HOLDINGS GROUP, INC.
(Exact name of registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of incorporation or organization)

75-2969997
(IRS Employer Identification No.)

200 CRESCENT COURT, SUITE 1200
DALLAS, TEXAS
75201
(Address of principal executive office)
(Zip Code)

(214) 756-6900
(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 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 definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

(Do not check if a 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 X

The number of shares of the issuer's common stock, par value \$0.01 per share, outstanding as of July 18, 2008:
6,972,458.

WESTWOOD HOLDINGS GROUP, INC.

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PART I - FINANCIAL INFORMATION

ITEM 1. UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETSAs of June 30, 2008 and December 31, 2007
(in thousands, except par value and share amounts)

	June 30, 2008 (unaudited)	December 31, 2007
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 5,009	\$ 4,560
Accounts receivable	4,169	6,599
Investments, at market value	23,038	22,144
Deferred income taxes	2,006	1,512
Other current assets	1,501	651
Total current assets	35,723	35,466
Goodwill	2,302	2,302
Deferred income taxes	267	225
Property and equipment, net of accumulated depreciation of \$1,116 and \$1,002	935	1,031
Total assets	\$ 39,227	\$ 39,024
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable and accrued liabilities	\$ 1,060	\$ 1,024
Dividends payable	2,091	1,702
Compensation and benefits payable	2,679	4,848
Income taxes payable	996	1,505
Other current liabilities	12	11
Total current liabilities	6,838	9,090
Deferred rent	519	588
Total liabilities	7,357	9,678
Stockholders' Equity:		
Common stock, \$0.01 par value, authorized 25,000,000 shares, issued 7,027,877 and outstanding 6,972,458 shares at June 30, 2008; authorized 10,000,000 shares, issued 6,840,327 and outstanding 6,807,408 shares at December 31, 2007	70	68
Additional paid-in capital	31,590	27,770
Treasury stock, at cost – 55,419 shares at June 30, 2008; 32,919 shares at December 31, 2007	(1,872)	(1,070)
Retained earnings	2,082	2,578
Total stockholders' equity	31,870	29,346
Total liabilities and stockholders' equity	\$ 39,227	\$ 39,024

See notes to interim consolidated financial statements.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except per share data)
(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2008	2007	2008	2007
REVENUES:				
Advisory fees				
Asset-based	\$ 6,606	\$ 5,003	\$ 12,996	\$ 9,586
Performance-based	80	-	80	
Trust fees	2,677	2,516	5,425	4,892
Other revenues, net	288	438	277	832
Total revenues	9,651	7,957	18,778	15,310
EXPENSES:				
Employee compensation and benefits	5,352	4,266	10,014	7,975
Sales and marketing	195	147	332	268
WHG mutual funds	106	66	141	101
Information technology	266	249	527	482
Professional services	439	379	887	779
General and administrative	695	609	1,266	1,125
Total expenses	7,053	5,716	13,167	10,730
Income before income taxes	2,598	2,241	5,611	4,580
Provision for income taxes	867	768	1,925	1,600
Net income	\$ 1,731	\$ 1,473	\$ 3,686	\$ 2,980
Earnings per share:				
Basic	\$ 0.29	\$ 0.26	\$ 0.61	\$ 0.52
Diluted	\$ 0.27	\$ 0.24	\$ 0.58	\$ 0.49

See notes to interim consolidated financial statements.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
For the Six Months Ended June 30, 2008
(in thousands)
(unaudited)

	Westwood Holdings Group, Inc. Common Stock, Par		Addi- tional Paid-In Capital	Treasury Stock	Retained Earnings	Total
	Shares	Amount				
BALANCE, January 1, 2008	6,807,408	\$ 68	\$ 27,770	\$ (1,070)	\$ 2,578	\$ 29,346
Net income					3,686	3,686
Issuance of restricted stock	183,800	2	(2)			-
Dividends declared (\$0.60 per share)					(4,182)	(4,182)
Restricted stock amortization			3,151			3,151
Tax benefit related to equity compensation			623			623
Stock options exercised	3,750	-	48			48
Purchase of treasury stock	(22,500)			(802)		(802)
BALANCE, June 30, 2008	6,972,458	\$ 70	\$ 31,590	\$ (1,872)	\$ 2,082	\$ 31,870

See notes to interim consolidated financial statements.

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WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)
(unaudited)

	For the six months ended June 30,	
	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 3,686	\$ 2,980
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	114	124
Unrealized (gains) and losses on investments	249	(20)
Restricted stock amortization	3,151	2,260
Deferred income taxes	(536)	(258)
Excess tax benefits from stock-based compensation	(450)	(176)
Net purchases of investments – trading securities	(69)	(778)
Change in operating assets and liabilities:		
Accounts receivable	2,430	357
Other current assets	(856)	102
Accounts payable and accrued liabilities	36	(79)
Compensation and benefits payable	(2,169)	(591)
Income taxes payable	114	476
Other liabilities	(14)	(3)
Net cash provided by operating activities	5,686	4,394
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of money market funds – available for sale	(3,478)	(3,986)
Sales of money market funds – available for sale	2,404	3,368
Purchase of property and equipment	(66)	(39)
Net cash used in investing activities	(1,140)	(657)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Purchase of treasury stock	(802)	(131)
Excess tax benefits from stock-based compensation	450	176
Proceeds from exercise of stock options	48	311
Cash dividends	(3,793)	(2,324)
Net cash used in financing activities	(4,097)	(1,968)
NET INCREASE IN CASH	449	1,769
Cash and cash equivalents, beginning of period	4,560	2,177
Cash and cash equivalents, end of period	\$ 5,009	\$ 3,946
Supplemental cash flow information:		
Cash paid during the period for income taxes	\$ 2,348	\$ 1,381
Issuance and (cancellation) of restricted stock	6,552	(59)
Tax benefit allocated directly to equity	623	282

See notes to interim consolidated financial statements.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. DESCRIPTION OF THE BUSINESS:

Westwood Holdings Group, Inc. ("Westwood," the "Company," "we," or "our") was incorporated under the laws of the State of Delaware on December 12, 2001, as a subsidiary of SWS Group, Inc. ("SWS"). On June 28, 2002, SWS completed the spin-off of Westwood by effecting a dividend distribution of all of the Westwood common stock held by SWS to all of its stockholders on a pro rata basis.

Westwood manages investment assets and provides services for its clients through two subsidiaries, Westwood Management Corp. ("Westwood Management") and Westwood Trust ("Westwood Trust"). Westwood Management provides investment advisory services to corporate pension funds, public retirement plans, endowments, foundations, and a family of mutual funds, which we call the WHG Funds, and investment subadvisory services to mutual funds and clients of Westwood Trust. Westwood Trust provides to institutions and high net worth individuals trust and custodial services and participation in common trust funds that it sponsors. Revenue is largely dependent on the total value and composition of assets under management ("AUM"). Accordingly, fluctuations in financial markets and in the composition of AUM impact revenue and results of operations.

Westwood Management is a registered investment advisor under the Investment Advisers Act of 1940. Westwood Trust is chartered and regulated by the Texas Department of Banking.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Basis of Presentation

The accompanying consolidated financial statements have been prepared without an audit and reflect all adjustments that, in the opinion of management, are necessary to present fairly our financial position as of June 30, 2008, and results of operations and cash flows for the periods presented. All such adjustments are normal and recurring in nature. The accompanying consolidated financial statements are presented using the accrual basis of accounting and have been prepared in accordance with the instructions for the presentation of interim financial information as prescribed by the Securities and Exchange Commission ("SEC") and, therefore, as permitted by SEC rules, do not contain certain information and footnote disclosures required by accounting principles generally accepted in the United States of America. The accompanying consolidated financial statements should be read in conjunction with our consolidated financial statements, and notes thereto, included in our Annual Report on Form 10-K for the year ended December 31, 2007. Refer to the accounting policies described in the notes to our annual financial statements, which were consistently followed in preparing this interim financial information. Operating results for the six months ended June 30, 2008 are not necessarily indicative of the results for the year ending December 31, 2008 or any future period.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, 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 reporting period. Actual results could differ from those estimates.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS---(Continued)
(Unaudited)

Revenue Recognition

Investment advisory and trust fees are recognized as services are provided. These fees are determined in accordance with contracts between our subsidiaries and their clients and are generally based on a percentage of AUM. A limited number of our clients have a performance-based fee component in their contract, which would pay us an additional fee if we outperform a specified index over a specific period of time. We would record as revenue any performance-based fees earned at the end of the performance period. Most advisory and trust fees are payable in advance or in arrears on a calendar quarterly basis. Advance payments are deferred and recognized over the periods services are performed. Since most of our advance paying clients' billing periods coincide with the calendar quarter to which payment relates, the revenue related to those clients is fully recognized within the quarter; consequently, there is not a significant amount of deferred revenue contained in these financial statements. Deferred revenue is shown on the balance sheet under the heading of "Other current liabilities". Other revenues generally consist of interest and investment income and unrealized gains and losses on our investments. These revenues are recognized as earned or as the services are performed.

Cash and Cash Equivalents

Cash and cash equivalents consist of short-term, highly liquid investments with maturities of three months or less.

Investments

Money market securities are classified as available for sale securities and have no significant fluctuating values. All other marketable securities are classified as trading securities. All securities are carried at quoted market value on the accompanying balance sheet. Net unrealized holding gains or losses on investments classified as trading securities are reflected as a component of other revenues. We measure realized gains and losses on investments using the specific identification method.

Goodwill

During the third quarter of 2007, we completed our annual impairment assessment as required by the Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No.142. No impairment loss was required. We perform our annual impairment assessment in the third quarter as of July 1.

Federal Income Taxes

We file a Federal income tax return as a consolidated group for Westwood and its subsidiaries. Deferred income tax assets and liabilities are determined based on the differences between the financial statement and income tax bases of assets and liabilities as measured at enacted income tax rates. Deferred income tax expense is generally the result of changes in the deferred tax assets and liabilities and relates primarily to stock-based compensation expense.

Fair Value of Financial Instruments

The estimated fair values of our financial instruments have been determined by us using available information. The fair value amounts discussed in Note 3 are not necessarily indicative of either the amounts we would realize upon disposition of these instruments or our intent or ability to dispose of these assets. The estimated fair value of cash and cash equivalents, as well as accounts receivable and payable, approximates their carrying value due to their short-term

maturities. The carrying amount of investments designated as “trading” securities, primarily U.S. Government and Government agency obligations as well as mutual funds and common trust fund shares, equals their fair value, which is equal to prices quoted in active markets and, with respect to funds, the net asset value of the shares held as reported by the fund. The carrying amount of investments designated as “available for sale” securities, primarily money market accounts, equals their fair value, which is equal to the net asset value of the shares held as reported by the fund. The market values of our money market holdings generally do not fluctuate.

Earnings per Share

Basic earnings per common share is computed by dividing net income available to common stockholders by the weighted average number of shares outstanding for the periods ended June 30, 2008 and 2007, respectively. Diluted earnings per share for these periods is computed based on the weighted average number of shares outstanding plus the effect of the dilutive impact of stock options and shares of restricted stock granted to employees and non-employee directors. Diluted earnings per common share is computed using the treasury stock method.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS---(Continued)
(Unaudited)

The following table sets forth the computation of basic and diluted shares (in thousands, except per share and share amounts):

	Three months ended June 30,		Six months ended June 30,	
	2008	2007	2008	2007
Net income	\$ 1,731	\$ 1,473	\$ 3,686	\$ 2,980
Weighted average shares outstanding – basic	6,014,074	5,767,238	6,020,074	5,761,409
Dilutive potential shares from stock options	35,950	43,474	36,047	44,872
Dilutive potential shares from restricted shares	362,274	329,713	334,680	316,950
Weighted average shares outstanding – diluted	6,412,298	6,140,425	6,390,801	6,123,231
Earnings per share:				
Basic	\$ 0.29	\$ 0.26	\$ 0.61	\$ 0.52
Diluted	\$ 0.27	\$ 0.24	\$ 0.58	\$ 0.49

Stock-Based Compensation

We account for stock-based compensation in accordance with FASB SFAS No. 123 Revised (“SFAS No. 123R”). Under SFAS No. 123R, stock-based compensation expense reflects the fair value of stock-based awards measured at grant date, is recognized over the relevant service period, and is adjusted each period for anticipated forfeitures. The compensation cost we record for these awards is based on their grant-date fair value as required by SFAS No. 123R.

We have issued restricted stock and stock options in accordance with our Third Amended and Restated Westwood Holdings Group, Inc. Stock Incentive Plan. We valued stock options issued based upon the Black-Scholes option-pricing model and recognized this value as an expense over the periods in which the options vested. Implementation of the Black-Scholes option-pricing model required us to make certain assumptions, including expected volatility, risk-free interest rate, expected dividend yield and expected life of the options. We utilized assumptions that we believed to be most appropriate at the time of the valuation. Had we used different assumptions in the pricing model, the expense recognized for stock options may have been different than the expense recognized in our financial statements. We must also apply judgment in developing an expectation of awards of restricted stock and stock options that may be forfeited. If actual experience differs significantly from these estimates, stock-based compensation expense and our results of operations could be materially affected.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS---(Continued)
(Unaudited)

3. INVESTMENTS:

Investment balances are presented in the table below (in thousands). All of these investments are carried at market value. The money market funds are accounted for as available for sale securities. The other investments are accounted for as trading securities.

	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
June 30, 2008:				
U.S. Government and Government agency obligations	\$ 1,969	\$ -	\$ -	\$ 1,969
Funds:				
Money market	16,191	-	-	16,191
Equity and fixed income	4,896	-	(18)	4,878
Marketable securities	\$ 23,056	\$ -	\$ (18)	\$ 23,038
December 31, 2007:				
U.S. Government and Government agency obligations	\$ 1,942	\$ 1	\$ -	\$ 1,943
Funds:				
Money market	15,117	-		