HOVNANIAN ENTERPRISES INC
Form 10-Q
June 05, 2009
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

[X] Quarterly report pursuant to Section 13 or 15(d) of the

Securities Exchange Act of 1934

For quarterly period ended APRIL 30, 2009

OR

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

Commission file number 1-8551

Hovnanian Enterprises, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	22-1851059
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

110 West Front Street, P.O. Box 500, Red Bank, NJ 07701

(Address of Principal Executive Offices) (Zip Code)

732-747-7800

(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 [X]   No [   ]

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. 62,617,464 shares of Class A Common Stock and 14,591,628 shares of Class B Common Stock were outstanding as of June 1, 2009.

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.

Large Accelerated Filer [   ] Accelerated Filer [X]
Non-Accelerated Filer [   ] (Do not check if smaller reporting company)   Smaller Reporting Company [   ]

HOVNANIAN ENTERPRISES, INC.

FORM 10-Q

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In Thousands Except Share Amounts)

ASSETS	April 30, 2009 (unaudited)	October 31, 2008 (1)
Homebuilding:		
Cash and cash equivalents	$779,178	$838,207
Restricted cash and cash equivalents	19,026	4,324
Inventories - at the lower of cost or fair value:		
Sold and unsold homes and lots under development	893,577	1,342,584
Land and land options held for future development or sale	493,105	644,067
Consolidated inventory not owned:		
Specific performance options	33,443	10,610
Variable interest entities	38,185	77,022
Other options	53,218	84,799
Total consolidated inventory not owned	124,846	172,431
Total inventories	1,511,528	2,159,082
Investments in and advances to unconsolidated joint ventures	42,170	71,097
Receivables, deposits, and notes	53,457	78,766
Property, plant, and equipment net	83,273	92,817
Prepaid expenses and other assets	134,234	156,595
Total homebuilding	2,622,866	3,400,888
Financial services:		
Cash and cash equivalents	3,958	9,849
Restricted cash	4,094	4,005
Mortgage loans held for sale or investment	59,273	90,729
Other assets	2,941	5,025
Total financial services	70,266	109,608
Income taxes receivable including net deferred tax benefits	-	126,826
Total assets	$2,693,132	$3,637,322

(1) Derived from the audited balance sheet as of October 31, 2008.

See notes to condensed consolidated financial statements (unaudited).

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In Thousands Except Share Amounts)

	April 30, 2009 (unaudited)	October 31, 2008 (1)
LIABILITIES AND STOCKHOLDERS EQUITY		
Homebuilding:		
Nonrecourse land mortgages	$820	$820
Accounts payable and other liabilities	319,739	420,695
Customers deposits	22,315	28,676
Nonrecourse mortgages secured by operating properties	21,911	22,302
Liabilities from inventory not owned	89,463	135,077
Total homebuilding	454,248	607,570
Financial services:		
Accounts payable and other liabilities	8,792	10,559
Mortgage warehouse line of credit	49,181	84,791
Total financial services	57,973	95,350
Notes payable:		
Revolving credit agreement	100,000	-
Senior secured notes	624,474	594,734
Senior notes	1,066,919	1,511,071
Senior subordinated notes	196,030	400,000
Accrued interest	65,026	72,477
Total notes payable	2,052,449	2,578,282
Income tax payable	40,427	-
Total liabilities	2,605,097	3,281,202
Minority interest related to inventory not owned	25,903	24,880
Minority interest in consolidated joint ventures	734	976
Stockholders equity:		
Preferred stock, $.01 par value - authorized 100,000 shares; issued 5,600 shares at April 30, 2009 and at October 31, 2008 with a liquidation preference of $140,000	135,299	135,299
Common stock, Class A, $.01 par value - authorized 200,000,000 shares; issued 74,250,353 shares at April 30, 2009 and 73,803,879 shares at October 31, 2008 (including 11,694,720 shares at April 30, 2009 and October 31, 2008 held in Treasury)	743	738
Common stock, Class B, $.01 par value (convertible to Class A at time of sale) - authorized 30,000,000 shares; issued 15,331,376 shares at April 30, 2009 and 15,331,494 shares at October 31, 2008 (including 691,748 shares at April 30, 2009 and October 31, 2008 held in Treasury)	153	153

Paid in capital - common stock	446,786	418,626
Accumulated deficit	(406,326)	(109,295)
Treasury stock - at cost	(115,257)	(115,257)
Total stockholders equity	61,398	330,264
Total liabilities and stockholders equity	$2,693,132	$3,637,322

(1) Derived from the audited balance sheet as of October 31, 2008.

See notes to condensed consolidated financial statements (unaudited).

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In Thousands Except Per Share Data)

(unaudited)

	Three Months Ended		Six Months Ended	
	April 30, 2009	2008	April 30, 2009	2008
Revenues:				
Homebuilding:				
Sale of homes	$381,698	$755,684	$740,750	$1,807,502
Land sales and other revenues	7,274	8,203	13,687	36,113
Total homebuilding	388,972	763,887	754,437	1,843,615
Financial services	9,027	12,552	17,346	26,525
Total revenues	397,999	776,439	771,783	1,870,140
Expenses:				
Homebuilding:				
Cost of sales, excluding interest	351,148	706,845	691,823	1,710,409
Cost of sales interest	26,040	34,572	49,169	63,160
Inventory impairment loss and land option write-offs	310,194	245,860	420,375	336,028
Total cost of sales	687,382	987,277	1,161,367	2,109,597
Selling, general and administrative	60,822	97,646	131,866	197,815
Total homebuilding	748,204	1,084,923	1,293,233	2,307,412
Financial services	6,510	8,450	13,258	19,320
Corporate general and administrative	18,359	20,530	49,269	41,685
Other interest	18,524	462	42,754	1,002
Other operations	4,935	1,823	6,559	3,290
Intangible amortization	-	292	-	1,227
Total expenses	796,532	1,116,480	1,405,073	2,373,936
Gain on extinguishment of debt	311,268	-	390,788	-
Loss from unconsolidated joint ventures	(10,094)	(3,397)	(32,683)	(8,436)
Loss before income taxes	(97,359)	(343,438)	(275,185)	(512,232)
State and federal income tax provision (benefit):				
State	21,221	11,942	21,776	14,225
Federal	41	(14,669)	70	(54,803)
Total taxes	21,262	(2,727)	21,846	(40,578)
Net loss	$(118,621)	$(340,711)	$(297,031)	$(471,654)
Per share data:				
Basic and assuming dilution:				

Loss per common share	$(1.50)	$(5.29)	$(3.80)	$(7.43)
Weighted average number of common shares outstanding	79,146	64,410	78,154	63,455

See notes to condensed consolidated financial statements (unaudited).

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY

(In Thousands Except Share Amounts)

(unaudited)

	A Common Stock		B Common Stock		Preferred Stock					
	Shares Issued and Outstanding	Amount	Shares Issued and Outstanding	Amount	Shares Issued and Outstanding	Amount	Paid-In Capital	Accumulated Deficit	Treasury Stock	Total
Balance, November 1, 2008	62,109,159	$738	14,639,746	$153	5,600	$135,299	$418,626	$(109,295)	$(115,257)	$330,264
Stock options amortization										
and issuances, net of tax							3,173			3,173
Stock option cancellations							12,269			12,269
Restricted stock										
amortization, issuances and										
forfeitures, net of tax	446,356	5					12,718			12,723
Conversion of Class B to Class A common stock	118		(118)							-
Net loss								(297,031)		(297,031)
Balance, April 30, 2009	62,555,633	$743	14,639,628	$153	5,600	$135,299	$446,786	$(406,326)	$(115,257)	$61,398

See notes to condensed consolidated financial statements (unaudited).

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Thousands)

(unaudited)

	Six Months Ended April 30, 2009	2008
Cash flows from operating activities:		
Net loss	$(297,031)	$(471,654)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation	9,286	9,105
Intangible amortization	-	1,227
Compensation from stock options and awards	8,943	8,709
Stock option cancellations	12,269	-
Amortization of bond discounts and deferred financing costs	620	232
Excess tax payments from share-based payment	-	2,243
Loss (gain) on sale and retirement of property and assets	108	(1,758)
Loss from unconsolidated joint ventures	32,683	8,436
Distributions of earnings from unconsolidated joint ventures	1,518	2,857
Gain on extinguishment of debt	(390,788)	-
Deferred income taxes	-	77,373
Impairment and land option write-offs	420,375	336,028
Decrease (increase) in assets:		
Mortgage notes receivable	31,467	46,387
Restricted cash, receivables, prepaids, deposits and other assets	34,498	23,277
Inventories	217,448	276,016
State and Federal income tax assets	126,826	(114,908)
(Decrease) increase in liabilities:		
State and Federal income tax liability	40,427	-
Customers deposits	(6,361)	(21,860)
Accounts payable, interest and other accrued liabilities	(138,222)	(131,612)
Net cash provided by operating activities	104,066	50,098
Cash flows from investing activities:		
Net proceeds from sale of property and assets	861	2,092
Purchase of property, equipment and other fixed assets and acquisitions	(262)	(3,376)
Investments in and advances to unconsolidated joint ventures	(9,660)	(9,262)
Distributions of capital from unconsolidated joint ventures	4,488	8,019
Net cash used in investing activities	(4,573)	(2,527)
Cash flows from financing activities:		
(Payments) proceeds from mortgages and notes	(453)	141
Net proceeds related to revolving credit agreement (includes deferred financing costs)	100,000	118,250
Net payments related to mortgage warehouse line of credit	(35,610)	(47,991)
Deferred financing costs from note issuances	(3,586)	-
Principal payments and debt repurchases	(224,764)	(9,112)
Excess tax payments from share-based payment	-	(2,243)
Net proceeds from sale of stock and employee stock plan	-	1,043
Net cash (used in) provided by financing activities	(164,413)	60,088
Net (decrease) increase in cash and cash equivalents	(64,920)	107,659
Cash and cash equivalents balance, beginning		

of period	848,056	16,233
Cash and cash equivalents balance, end of period	$783,136	$123,892

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Thousands - Unaudited)

(Continued)

	Six Months Ended April 30, 2009	2008
Supplemental disclosures of cash flow:		
Cash paid (received) during the period for:		
Interest, net of capitalized interest	$96,763	$69,144
Income taxes	$(145,408)	$(3,956)

Supplemental disclosure of noncash financing activities:

In the first quarter of fiscal 2009, the Company issued $29.3 million of 18.0% Senior Secured Notes due 2017 in exchange for $71.4 million of unsecured senior notes.

See notes to condensed consolidated financial statements (unaudited).

HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED

Hovnanian Enterprises, Inc. (the Company , the Parent , we , us or our) has reportable segments consisting of six Homebuilding segments (Northeast, Mid-Atlantic, Midwest, Southeast, Southwest and West) and the Financial Services segment (see Note 15).

The accompanying unaudited Condensed Consolidated Financial Statements include our accounts and those of all wholly-owned subsidiaries after elimination of all intercompany balances and transactions. Certain prior year amounts have been reclassified to conform to the current year presentation.

1. The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments for interim periods presented have been made, which include normal recurring accruals and deferrals necessary for a fair presentation of our consolidated financial position, results of operations, and cash flows. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates, and these differences could have a significant impact on the financial statements. Results for interim periods are not necessarily indicative of the results which might be expected for a full year. The balance sheet at October 31, 2008 has been derived from the audited Consolidated Financial Statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements.

2. For the three and six months ended April 30, 2009, the Company s total stock-based compensation expense was $4.4 million (net of tax) and $21.2 million (net of tax), respectively. Included in this total stock-based compensation expense was the vesting of stock options of $1.5 million (net of tax) and $3.2 million (net of tax) for the three and six months ended April 30, 2009, respectively. Also included in the six months ended April 30, 2009 is $12.3 million (net of tax) for stock option cancellations that occurred in the first quarter of fiscal 2009. The Chief Executive Officer, Chief Financial Officer and each of the non-executive Board of Directors consented to the cancellation of certain of their options (with the full understanding that the Company made no commitment to provide them with any other form of consideration in respect to the cancelled options) in order to reduce a portion of the equity reserve overhang under the Company s equity compensation plans represented by the number of shares of the Company s common stock remaining available for future issuance under such plans (including shares that may be issued upon the exercise or vesting of outstanding options and other rights).

3. Interest costs incurred, expensed and capitalized were:

	Three Months Ended April 30,		Six Months Ended April 30,	
(In thousands)	2009	2008	2009	2008
Interest capitalized at beginning of period	$176,258	$171,430	$170,107	$155,642
Plus interest incurred (1)	47,588	41,206	101,098	86,122
Less cost of sales interest expensed	26,040	34,572	49,169	63,160
Less other interest expensed(2)	18,524	462	42,754	1,002
Interest capitalized at end of period (3)	$179,282	$177,602	$179,282	$177,602

(1) Data does not include interest incurred by our mortgage and finance subsidiaries.

(2) Beginning in the third quarter of fiscal 2008, our assets that qualify for interest capitalization (inventory

under development) no longer exceed our debt, and therefore the portion of interest not covered by qualifying assets must be directly expensed. In addition, interest on completed homes and land in planning, which does not qualify for capitalization is expensed as incurred.

(3) We have incurred significant inventory impairments in recent years, which are determined based on

total inventory including capitalized interest. However, the capitalized interest amounts shown above are gross amounts before allocating any portion of the impairments to capitalized interest.

4. Accumulated depreciation at April 30, 2009 and October 31, 2008 amounted to $77.6 million and $70.5 million, respectively, for our homebuilding property, plant and equipment.

5. In accordance with Financial Accounting Standards Board Statement No. 144 ("SFAS 144"), *Accounting for the Impairment or Disposal of Long Lived Assets*, we record impairment losses on inventories related to communities under development and held for future development when events and circumstances indicate that they may be impaired and the undiscounted cash flows estimated to be generated by those assets are less than their related carrying amounts. If the expected undiscounted cash flows are less than the carrying amount, then the community is written down to its fair value. We estimated the fair value of each impaired community by determining the present value of the estimated future cash flows at a discount rate commensurate with the risk of the respective community. For the six months ended April 30, 2009, our discount rates used for the impairments recorded range from 14.3% to 16.5%. Should the estimates or expectations used in determining cash flows or fair value decrease or differ from current estimates in the future, we may be required to recognize additional impairments. As a result of a continued decline in sales price and general market conditions in certain markets we recorded inventory impairments, for the three months ended April 30, 2009 and 2008, of $301.1 million and $226.4 million, respectively, and for the six months ended April 30, 2009 and 2008, of $396.8 million and $300.2 million, respectively, each of which are presented in the Condensed Consolidated Statements of Operations as part of Inventory impairment loss and land option write-offs and deducted from inventories as presented in the Condensed Consolidated Balance Sheets.

The following table represents inventory impairments by homebuilding segment for the three and six months ended April 30, 2009 and 2008:

(Dollars in millions)	Three Months Ended April 30, 2009			Three Months Ended April 30, 2008		
	Number of Communities	Dollar Amount of Impairment	Pre-Impairment Value(1)	Number of Communities	Dollar Amount of Impairment	Pre-Impairment Value(1)
Northeast	8	$108.0	$175.7	6	$12.3	$86.1
Mid-Atlantic	24	13.4	54.3	6	8.3	32.9
Midwest	4	4.0	12.0	-	-	-
Southeast	41	17.6	49.9	12	11.4	43.5
Southwest	29	23.4	52.3	14	17.3	40.7
West	37	134.7	255.7	45	177.1	464.9
Total	143	$301.1	$599.9	83	$226.4	$668.1

(Dollars in millions)	Six Months Ended April 30, 2009			Six Months Ended April 30, 2008		
	Number of Communities	Dollar Amount of Impairment	Pre-Impairment Value(1)	Number of Communities	Dollar Amount of Impairment	Pre-Impairment Value(1)
Northeast	19	$161.6	$326.8	6	$14.8	$105.8
Mid-Atlantic	37	26.3	95.3	10	11.6	51.6
Midwest	4	4.0	12.0	4	5.6	20.2

Southeast	56	25.5	82.3	15	17.8	71.8
Southwest	34	26.4	63.1	16	22.1	57.8
West	40	153.0	299.5	52	228.3	680.2
Total	190	$396.8	$879.0	103	$300.2	$987.4

(1) Represents carrying value in dollars, net of prior period impairments, if any, at the time of recording

this period s impairments.

The Condensed Consolidated Statements of Operations line entitled "Inventory impairment loss and land option write-offs" also includes write-offs of capitalized approval, engineering and interest costs that we record when we redesign communities and/or abandon certain engineering costs or when we do not intend to exercise options (walk-away) in various locations because the communities' projected profitability will not produce adequate returns on investment commensurate with the risk. The total aggregate write-offs were $9.1 million and $19.5 million for the three months ended April 30, 2009 and 2008, respectively, and $23.6 million and $35.8 million for the six months ended April 30, 2009 and 2008, respectively.

The following table represents write-offs of such costs and the related number of lots by homebuilding segment for the three and six months ended April 30, 2009 and 2008:

(Dollars in millions)	Three Months Ended April 30,				Six Months Ended April 30,			
	2009		2008		2009		2008	
	Number of Walk-Away Lots	Dollar Amount of Write-Offs	Number of Walk-Away Lots	Dollar Amount of Write-Offs	Number of Walk-Away Lots	Dollar Amount of Write-Offs	Number of Walk-Away Lots	Dollar Amount of Write-Offs
Northeast	103	$2.2	144	$3.0	606	$6.5	453	$4.7
Mid-Atlantic	452	2.3	1,755	4.4	1,902	8.5	2,528	15.8
Midwest	158	1.4	-	-	158	1.4	-	-
Southeast	-	(0.4)	1,405	6.8	153	(0.1)	1,754	7.2
Southwest	474	3.3	202	1.6	758	6.7	430	4.4
West	-	0.3	239	3.7	-	0.6	239	3.7
Total	1,187	$9.1	3,745	$19.5	3,577	$23.6	5,404	$35.8

As a result of the declining homebuilding market in some of our segments, we have decided to mothball (or stop development on) certain communities where we have determined the current performance does not justify further investment at this time. When we decide to mothball a community, the inventory is reclassified from Sold and unsold homes and lots under development to Land and land options held for future development or sale . During the second quarter of fiscal 2009, we mothballed 12 communities with an aggregate book value of $43.6 million, net of an impairment reserve balance of $26.5 million. As of April 30, 2009, the book value associated with our 76 total mothballed communities was $388.4 million, net of an impairment reserve balance of $499.4 million.

6. We establish a warranty accrual for repair costs under $5,000 per occurrence to homes, community amenities and land development infrastructure. We accrue for warranty costs as part of cost of sales at the time each home is closed and title and possession have been transferred to the homebuyer. In addition, we accrue for warranty costs over $5,000 per occurrence as part of our general liability insurance deductible, which is expensed as selling, general and administrative costs. For homes delivered in fiscal 2009 and 2008, our deductible under our general liability insurance is $20 million per occurrence with an aggregate $20 million for liability claims and an aggregate $21.5 million for construction defect claims. Additions and charges in the warranty reserve and general liability accrual for the three and six months ended April 30, 2009 and 2008 were as follows:

(In thousands)	Three Months Ended April 30, 2009	2008	Six Months Ended April 30, 2009	2008
Balance, beginning of period	$125,976	$120,855	$125,738	$120,653
Additions	9,533	20,507	21,047	34,807
Charges incurred	(16,622)	(17,796)	(27,898)	(31,894)
Balance, end of period	$118,887	$123,566	$118,887	$123,566

Warranty accruals are based upon historical experience. We engage a third-party actuary that uses our historical warranty data to estimate our unpaid claims, claim adjustment expenses and incurred but not reported claims reserves for the risks that we are assuming under the general liability and workers compensation programs. The estimates include provisions for inflation, claims handling and legal fees.

Insurance claims paid by our insurance carriers were $9.2 million and $2.1 million for the three months ended April 30, 2009 and 2008, respectively, and $19.5 million and $7.0 million for the six months ended April 30, 2009 and 2008, respectively, for prior year deliveries.

7. We are involved in litigation arising in the ordinary course of business, none of which is expected to have a material adverse effect on our financial position or results of operations, and we are subject to extensive and complex regulations that affect the development and home building, sales and customer financing processes, including zoning, density, building standards and mortgage financing. These regulations often provide broad discretion to the administering governmental authorities. This can delay or increase the cost of development or homebuilding.

We also are subject to a variety of local, state, federal and foreign laws and regulations concerning protection of health and the environment. The particular environmental laws that apply to any given community vary greatly according to the community site, the site s environmental conditions and the present and former uses of the site. These environmental laws may result in delays, may cause us to incur substantial compliance, remediation and/o