

MDC HOLDINGS INC  
Form 10-Q  
April 30, 2019

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

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**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 March 31, 2019**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**Commission File No. 1-8951**

**M.D.C. HOLDINGS, INC.**

**(Exact name of Registrant as specified in its charter)**

Delaware  
(State or other jurisdiction  
of incorporation or organization)

84-0622967  
(I.R.S.  
employer  
identification  
no.)

4350 South Monaco Street, Suite 500 80237  
Denver, Colorado (Zip code)  
(Address of principal executive offices)  
(303) 773-1100

(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 every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See definition of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer Accelerated Filer  
Non-Accelerated Filer Smaller Reporting Company  
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of April 29, 2019, 61,520,890 shares of M.D.C. Holdings, Inc. common stock were outstanding.

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**M.D.C. HOLDINGS, INC.**

**FORM 10-Q**

**FOR THE QUARTER ENDED MARCH 31, 2019**

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(i)

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Table of Contents**PART I****ITEM 1. Unaudited Consolidated Financial Statements****M.D.C. HOLDINGS, INC.****Consolidated Balance Sheets**

|                                         | March 31,<br>2019                                      | December<br>31,<br>2018 |
|-----------------------------------------|--------------------------------------------------------|-------------------------|
|                                         | (Dollars in thousands,<br>except per<br>share amounts) |                         |
| <b>ASSETS</b>                           |                                                        |                         |
| <b>Homebuilding:</b>                    |                                                        |                         |
| Cash and cash equivalents               | \$416,374                                              | \$414,724               |
| Restricted cash                         | 8,136                                                  | 6,363                   |
| Trade and other receivables             | 67,960                                                 | 52,982                  |
| Inventories:                            |                                                        |                         |
| Housing completed or under construction | 950,274                                                | 952,436                 |
| Land and land under development         | 1,198,824                                              | 1,180,558               |
| Total inventories                       | 2,149,098                                              | 2,132,994               |
| Property and equipment, net             | 59,765                                                 | 58,167                  |
| Operating lease right-of-use asset      | 32,604                                                 | -                       |
| Deferred tax asset, net                 | 34,504                                                 | 37,178                  |
| Prepaid and other assets                | 42,545                                                 | 45,794                  |
| Total homebuilding assets               | 2,810,986                                              | 2,748,202               |
| <b>Financial Services:</b>              |                                                        |                         |
| Cash and cash equivalents               | 51,556                                                 | 49,052                  |
| Marketable securities                   | 45,767                                                 | 40,879                  |
| Mortgage loans held-for-sale, net       | 110,810                                                | 149,211                 |
| Other assets                            | 15,800                                                 | 13,733                  |
| Total financial services assets         | 223,933                                                | 252,875                 |
| Total Assets                            | \$3,034,919                                            | \$3,001,077             |
| <b>LIABILITIES AND EQUITY</b>           |                                                        |                         |
| <b>Homebuilding:</b>                    |                                                        |                         |
| Accounts payable                        | \$58,570                                               | \$50,505                |
| Accrued liabilities                     | 185,131                                                | 196,247                 |
| Operating lease liability               | 33,460                                                 | -                       |
| Revolving credit facility               | 15,000                                                 | 15,000                  |

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|                                                                                                                                                                       |             |             |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------|-------------|
| Senior notes, net                                                                                                                                                     | 988,322     | 987,967     |
| Total homebuilding liabilities                                                                                                                                        | 1,280,483   | 1,249,719   |
| <b>Financial Services:</b>                                                                                                                                            |             |             |
| Accounts payable and accrued liabilities                                                                                                                              | 58,874      | 58,543      |
| Mortgage repurchase facility                                                                                                                                          | 84,856      | 116,815     |
| Total financial services liabilities                                                                                                                                  | 143,730     | 175,358     |
| Total Liabilities                                                                                                                                                     | 1,424,213   | 1,425,077   |
| <b>Stockholders' Equity</b>                                                                                                                                           |             |             |
| Preferred stock, \$0.01 par value; 25,000,000 shares authorized; none issued or outstanding                                                                           | -           | -           |
| Common stock, \$0.01 par value; 250,000,000 shares authorized; 61,520,890 and 56,615,352 issued and outstanding at March 31, 2019 and December 31, 2018, respectively | 615         | 566         |
| Additional paid-in-capital                                                                                                                                            | 1,318,726   | 1,168,442   |
| Retained earnings                                                                                                                                                     | 291,365     | 406,992     |
| Total Stockholders' Equity                                                                                                                                            | 1,610,706   | 1,576,000   |
| Total Liabilities and Stockholders' Equity                                                                                                                            | \$3,034,919 | \$3,001,077 |

The accompanying Notes are an integral part of these Unaudited Consolidated Financial Statements.

Table of Contents**M.D.C. HOLDINGS, INC.****Consolidated Statements of Operations and Comprehensive Income**

|                                                 | Three Months Ended<br>March 31,                     |            |
|-------------------------------------------------|-----------------------------------------------------|------------|
|                                                 | 2019                                                | 2018       |
|                                                 | (Dollars in thousands,<br>except per share amounts) |            |
| <b>Homebuilding:</b>                            |                                                     |            |
| Home sale revenues                              | \$647,278                                           | \$607,688  |
| Home cost of sales                              | (524,552 )                                          | (496,632 ) |
| Inventory impairments                           | (610 )                                              | (550 )     |
| Total cost of sales                             | (525,162 )                                          | (497,182 ) |
| Gross profit                                    | 122,116                                             | 110,506    |
| Selling, general and administrative expenses    | (82,261 )                                           | (71,341 )  |
| Interest and other income                       | 2,391                                               | 1,859      |
| Other expense                                   | (1,191 )                                            | (563 )     |
| Homebuilding pretax income                      | 41,055                                              | 40,461     |
| <b>Financial Services:</b>                      |                                                     |            |
| Revenues                                        | 17,404                                              | 19,035     |
| Expenses                                        | (8,957 )                                            | (8,831 )   |
| Interest and other income                       | 1,264                                               | 1,020      |
| Net gain (loss) on marketable equity securities | 4,840                                               | (1,153 )   |
| Financial services pretax income                | 14,551                                              | 10,071     |
| Income before income taxes                      | 55,606                                              | 50,532     |
| Provision for income taxes                      | (15,056 )                                           | (11,768 )  |
| Net income                                      | \$40,550                                            | \$38,764   |
| Other comprehensive income                      | -                                                   | -          |
| Comprehensive income                            | \$40,550                                            | \$38,764   |
| Earnings per share:                             |                                                     |            |
| Basic                                           | \$0.66                                              | \$0.64     |
| Diluted                                         | \$0.64                                              | \$0.63     |
| Weighted average common shares outstanding:     |                                                     |            |
| Basic                                           | 60,939,364                                          | 60,340,774 |
| Diluted                                         | 62,708,334                                          | 61,447,563 |
| Dividends declared per share                    | \$0.30                                              | \$0.28     |



The accompanying Notes are an integral part of these Unaudited Consolidated Financial Statements.

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(Dollars in thousands, except share amounts)

|                                                                             | Three-Month Period Ended March 31, 2019 |        |                                  |                      |                                                 |             |
|-----------------------------------------------------------------------------|-----------------------------------------|--------|----------------------------------|----------------------|-------------------------------------------------|-------------|
|                                                                             | Common Stock                            |        | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income | Total       |
|                                                                             | Shares                                  | Amount |                                  |                      |                                                 |             |
| Balance at December 31, 2018                                                | 56,615,352                              | \$ 566 | \$1,168,442                      | \$406,992            | \$ -                                            | \$1,576,000 |
| Cumulative effect of newly adopted accounting standards (Note 2)            | -                                       | -      | -                                | (67 )                | -                                               | (67 )       |
| Balance at January 1, 2019                                                  | 56,615,352                              | 566    | 1,168,442                        | 406,925              | -                                               | 1,575,933   |
| Net Income                                                                  | -                                       | -      | -                                | 40,550               | -                                               | 40,550      |
| Shares issued upon exercise of stock options and awards of restricted stock | 372,344                                 | 4      | 7,083                            | -                    | -                                               | 7,087       |
| Cash dividends declared                                                     | -                                       | -      | -                                | (17,019 )            | -                                               | (17,019 )   |
| Stock dividend declared                                                     | 4,534,908                               | 45     | 138,950                          | (139,091)            | -                                               | (96 )       |
| Stock-based compensation expense                                            | -                                       | -      | 4,251                            | -                    | -                                               | 4,251       |
| Forfeiture of restricted stock                                              | (1,714 )                                | -      | -                                | -                    | -                                               | -           |
| Balance at March 31, 2019                                                   | 61,520,890                              | \$ 615 | \$1,318,726                      | \$291,365            | \$ -                                            | \$1,610,706 |

|                                                                             | Three-Month Period Ended March 31, 2018 |        |                                  |                      |                                                 |             |
|-----------------------------------------------------------------------------|-----------------------------------------|--------|----------------------------------|----------------------|-------------------------------------------------|-------------|
|                                                                             | Common Stock                            |        | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income | Total       |
|                                                                             | Shares                                  | Amount |                                  |                      |                                                 |             |
| Balance at December 31, 2017                                                | 56,123,228                              | \$ 561 | \$1,144,570                      | \$258,164            | \$ 3,992                                        | \$1,407,287 |
| Cumulative effect of newly adopted accounting standards                     | -                                       | -      | -                                | 5,766                | (3,992 )                                        | 1,774       |
| Balance at January 1, 2018                                                  | 56,123,228                              | 561    | 1,144,570                        | 263,930              | -                                               | 1,409,061   |
| Net Income                                                                  | -                                       | -      | -                                | 38,764               | -                                               | 38,764      |
| Shares issued upon exercise of stock options and awards of restricted stock | 97,783                                  | 1      | 281                              | -                    | -                                               | 282         |
| Cash dividends declared                                                     | -                                       | -      | -                                | (16,865 )            | -                                               | (16,865 )   |
| Stock-based compensation expense                                            | -                                       | -      | 1,251                            | -                    | -                                               | 1,251       |
| Forfeiture of restricted stock                                              | (1,368 )                                | -      | -                                | -                    | -                                               | -           |
| Balance at March 31, 2018                                                   | 56,219,643                              | \$ 562 | \$1,146,102                      | \$285,829            | \$ -                                            | \$1,432,493 |

The accompanying Notes are an integral part of these Unaudited Consolidated Financial Statements.

Table of Contents**M.D.C. HOLDINGS, INC.****Consolidated Statements of Cash Flows**

|                                                                                             | Three Months Ended<br>March 31, |           |
|---------------------------------------------------------------------------------------------|---------------------------------|-----------|
|                                                                                             | 2019                            | 2018      |
|                                                                                             | (Dollars in thousands)          |           |
| <b>Operating Activities:</b>                                                                |                                 |           |
| Net income                                                                                  | \$40,550                        | \$38,764  |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: |                                 |           |
| Stock-based compensation expense                                                            | 4,251                           | 1,251     |
| Depreciation and amortization                                                               | 4,878                           | 4,636     |
| Inventory impairments                                                                       | 610                             | 550       |
| Net (gain) loss on marketable equity securities                                             | (4,840 )                        | 1,153     |
| Amortization of discount / premiums on marketable debt securities, net                      | -                               | (182 )    |
| Deferred income tax expense                                                                 | 2,696                           | 423       |
| Net changes in assets and liabilities:                                                      |                                 |           |
| Trade and other receivables                                                                 | (13,771 )                       | (3,261 )  |
| Mortgage loans held-for-sale, net                                                           | 38,401                          | 24,956    |
| Housing completed or under construction                                                     | 2,137                           | (65,378 ) |
| Land and land under development                                                             | (18,496 )                       | (71,552 ) |
| Prepaid and other assets                                                                    | 1,085                           | 389       |
| Accounts payable and accrued liabilities                                                    | (3,153 )                        | 6,765     |
| Net cash provided by (used in) operating activities                                         | 54,348                          | (61,486 ) |
| <b>Investing Activities:</b>                                                                |                                 |           |
| Purchases of marketable securities                                                          | (4,785 )                        | (8,761 )  |
| Sales of marketable securities                                                              | 4,737                           | 8,700     |
| Purchases of property and equipment                                                         | (6,386 )                        | (6,316 )  |
| Net cash used in investing activities                                                       | (6,434 )                        | (6,377 )  |
| <b>Financing Activities:</b>                                                                |                                 |           |
| Payments on mortgage repurchase facility, net                                               | (31,959 )                       | (22,214 ) |
| Dividend payments                                                                           | (17,115 )                       | (16,865 ) |
| Proceeds from exercise of stock options                                                     | 7,087                           | 282       |
| Net cash used in financing activities                                                       | (41,987 )                       | (38,797 ) |
| Net increase (decrease) in cash, cash equivalents and restricted cash                       | 5,927                           | (106,660) |
| Cash, cash equivalents and restricted cash:                                                 |                                 |           |
| Beginning of period                                                                         | 470,139                         | 514,240   |
| End of period                                                                               | \$476,066                       | \$407,580 |
| <b>Reconciliation of cash, cash equivalents and restricted cash:</b>                        |                                 |           |
| Homebuilding:                                                                               |                                 |           |

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|                                                  |           |           |
|--------------------------------------------------|-----------|-----------|
| Cash and cash equivalents                        | \$416,374 | \$352,868 |
| Restricted cash                                  | 8,136     | 6,198     |
| Financial Services:                              |           |           |
| Cash and cash equivalents                        | 51,556    | 48,514    |
| Total cash, cash equivalents and restricted cash | \$476,066 | \$407,580 |

The accompanying Notes are an integral part of these Unaudited Consolidated Financial Statements.

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**1. Basis of Presentation**

The Unaudited Consolidated Financial Statements of M.D.C. Holdings, Inc. ("MDC," "the Company," "we," "us," or "our," which refers to M.D.C. Holdings, Inc. and its subsidiaries) have been prepared, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). Accordingly, they do not include all information and footnotes required by U.S. generally accepted accounting principles ("GAAP") for complete financial statements. These statements reflect all normal and recurring adjustments which, in the opinion of management, are necessary to present fairly the financial position, results of operations and cash flows of MDC at March 31, 2019 and for all periods presented. These statements should be read in conjunction with MDC's Consolidated Financial Statements and Notes thereto included in MDC's Annual Report on Form 10-K for the year ended December 31, 2018.

On January 28, 2019, MDC's board of directors declared an 8% stock dividend that was distributed on February 28, 2019 to shareholders of record on February 14, 2019. In accordance with Accounting Standards Codification ("ASC") Topic 260, *Earnings Per Share* ("ASC 260"), basic and diluted earnings per share amounts, share amounts and dividends declared per share have been restated for any periods or dates prior to the stock dividend record date.

Included in these footnotes are certain statements that constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include statements regarding our business, financial condition, results of operations, cash flows, strategies and prospects. These forward-looking statements may be identified by terminology such as "likely," "may," "will," "should," "expects," "plans," "anticipates," "believes," "estimates," "predicts," "potential" or "continue," or the negative of such terms and other comparable terminology. Although we believe that the expectations reflected in the forward-looking statements contained in this section are reasonable, we cannot guarantee future results. These statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company to be materially different from those expressed or implied by the forward-looking statements. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise. However, any further disclosures made on related subjects in subsequent reports on Forms 10-K, 10-Q and 8-K should be considered.

Where necessary, reclassifications have been made to our prior period financial information to conform to the current year presentation.

**2. Recently Issued Accounting Standards**

**Adoption of New Accounting Standards**

Accounting Standards Update (“ASU”) 2016-02, *Leases* (“ASU 2016-02”) is codified in ASC 842, *Leases* (“ASC 842”). ASC 842 supersedes current lease guidance in ASC 840 and requires a lessee to recognize a right-of-use asset and a corresponding lease liability for substantially all leases. The lease liability will be equal to the present value of the remaining lease payments while the right-of-use asset will be similarly calculated and then adjusted for initial direct costs. In addition, ASC 842 expands the disclosure requirements to increase the transparency and comparability of the amount, timing and uncertainty of cash flows arising from leases. On January 1, 2019, we adopted ASC 842 using the modified retrospective transition method. We elected available practical expedients permitted under the transition guidance within the new standard, which among other items, allowed the Company to carry forward its historical lease classification and not reassess existing leases under the new definition of a lease in ASC 842. In addition, we will account for lease and non-lease components as a single lease component.

Adoption of ASC 842 resulted in the recording of additional net lease assets and lease liabilities of \$34.2 million and \$34.3 million, respectively, as of January 1, 2019. The difference between the additional lease assets and lease liabilities, net of the deferred tax impact, was recorded as an adjustment to retained earnings. The standard did not materially impact our consolidated statements of operations and comprehensive income or consolidated cash flows.

#### **Accounting Standards Issued But Not Yet Adopted**

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments—Credit Losses (Topic 326) Measurement of Credit Losses on Financial Instruments* (“ASU 2016-13”), which requires measurement and recognition of expected credit losses for financial assets held. The amendments in ASU 2016-13 eliminate the probable threshold for initial recognition of a credit loss in current GAAP and reflect an entity’s current estimate of all expected credit losses. ASU 2016-13 is effective for our interim and annual reporting periods beginning January 1, 2020, and is to be applied using a modified retrospective transition method. Earlier adoption is permitted. We do not plan to early adopt ASU 2016-13 and with our current holdings of financial instruments that are subject to credit losses, we do not believe adoption of this guidance will be material to our financial statements.

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**3. Segment Reporting**

An operating segment is defined as a component of an enterprise for which discrete financial information is available and is reviewed regularly by the Chief Operating Decision Maker (“CODM”), or decision-making group, to evaluate performance and make operating decisions. We have identified our CODM as two key executives—the Chief Executive Officer (“CEO”) and the Chief Operating Officer (“COO”).

We have identified each homebuilding division as an operating segment. Our homebuilding operating segments have been aggregated into the reportable segments noted below because they are similar in the following regards: (1) economic characteristics; (2) housing products; (3) class of homebuyer; (4) regulatory environments; and (5) methods used to construct and sell homes. Our homebuilding reportable segments are as follows:

West (Arizona, California, Nevada, Washington and Oregon)  
Mountain (Colorado and Utah)  
East (mid-Atlantic, which includes Virginia and Maryland, and Florida)

Our financial services business consists of the operations of the following operating segments: (1) HomeAmerican Mortgage Corporation (“HomeAmerican”); (2) Allegiant Insurance Company, Inc., A Risk Retention Group (“Allegiant”); (3) StarAmerican Insurance Ltd. (“StarAmerican”); (4) American Home Insurance Agency, Inc.; and (5) American Home Title and Escrow Company. Due to its contributions to consolidated pretax income, we consider HomeAmerican to be a reportable segment (“mortgage operations”). The remaining operating segments have been aggregated into one reportable segment (“other”) because they do not individually exceed 10 percent of: (1) consolidated revenue; (2) the greater of (a) the combined reported profit of all operating segments that did not report a loss or (b) the positive value of the combined reported loss of all operating segments that reported losses; or (3) consolidated assets.

Corporate is a non-operating segment that develops and implements strategic initiatives and supports our operating divisions by centralizing key administrative functions such as finance, treasury, information technology, insurance, risk management, litigation and human resources. Corporate also provides the necessary administrative functions to support MDC as a publicly traded company. A portion of the expenses incurred by Corporate are allocated to the homebuilding operating segments based on their respective percentages of assets, and to a lesser degree, a portion of Corporate expenses are allocated to the financial services segments. A majority of Corporate’s personnel and resources are primarily dedicated to activities relating to the homebuilding segments, and, therefore, the balance of any unallocated Corporate expenses is included in the homebuilding operations section of our consolidated statements of operations and comprehensive income.

The following table summarizes revenues for our homebuilding and financial services operations:



|                                   | Three Months Ended<br>March 31,<br>2019      2018<br>(Dollars in<br>thousands) |           |
|-----------------------------------|--------------------------------------------------------------------------------|-----------|
| <b>Homebuilding</b>               |                                                                                |           |
| West                              | \$369,558                                                                      | \$319,509 |
| Mountain                          | 209,192                                                                        | 208,632   |
| East                              | 68,528                                                                         | 79,547    |
| Total homebuilding revenues       | \$647,278                                                                      | \$607,688 |
| <b>Financial Services</b>         |                                                                                |           |
| Mortgage operations               | \$10,174                                                                       | \$12,696  |
| Other                             | 7,230                                                                          | 6,339     |
| Total financial services revenues | \$17,404                                                                       | \$19,035  |

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The following table summarizes pretax income (loss) for our homebuilding and financial services operations:

|                                        | Three Months<br>Ended<br>March 31,<br>2019      2018<br>(Dollars in<br>thousands) |          |
|----------------------------------------|-----------------------------------------------------------------------------------|----------|
| <b>Homebuilding</b>                    |                                                                                   |          |
| West                                   | \$33,200                                                                          | \$24,373 |
| Mountain                               | 21,714                                                                            | 24,185   |
| East                                   | 1,473                                                                             | 3,375    |
| Corporate                              | (15,332)                                                                          | (11,472) |
| Total homebuilding pretax income       | \$41,055                                                                          | \$40,461 |
| <b>Financial Services</b>              |                                                                                   |          |
| Mortgage operations                    | \$4,993                                                                           | \$7,520  |
| Other                                  | 9,558                                                                             | 2,551    |
| Total financial services pretax income | \$14,551                                                                          | \$10,071 |
| Total pretax income                    | \$55,606                                                                          | \$50,532 |

The following table summarizes total assets for our homebuilding and financial services operations. The assets in our West, Mountain and East segments consist primarily of inventory while the assets in our Corporate segment primarily include our cash and cash equivalents and deferred tax assets. The assets in our financial services segment consist mostly of cash and cash equivalents, marketable securities and mortgage loans held-for-sale.

|                                  | March 31,<br>2019 | December<br>31,<br>2018<br>(Dollars in thousands) |
|----------------------------------|-------------------|---------------------------------------------------|
| <b>Homebuilding assets</b>       |                   |                                                   |
| West                             | \$1,307,761       | \$1,301,374                                       |
| Mountain                         | 818,451           | 793,150                                           |
| East                             | 170,670           | 169,485                                           |
| Corporate                        | 514,104           | 484,193                                           |
| Total homebuilding assets        | \$2,810,986       | \$2,748,202                                       |
| <b>Financial services assets</b> |                   |                                                   |
| Mortgage operations              | \$123,139         | \$159,677                                         |
| Other                            | 100,794           | 93,198                                            |
| Total financial services assets  | \$223,933         | \$252,875                                         |

Total assets                      \$3,034,919    \$3,001,077

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Table of Contents**4. Earnings Per Share**

ASC 260 requires a company that has participating security holders (for example, holders of unvested restricted stock that have non-forfeitable dividend rights) to utilize the two-class method for calculating earnings per share (“EPS”) unless the treasury stock method results in lower EPS. The two-class method is an allocation of earnings/(loss) between the holders of common stock and a company’s participating security holders. Under the two-class method, earnings/(loss) for the reporting period are allocated between common shareholders and other security holders based on their respective rights to receive distributed earnings (i.e., dividends) and undistributed earnings (i.e., net income/(loss)). Our common shares outstanding are comprised of shareholder owned common stock and shares of unvested restricted stock held by participating security holders. Basic EPS is calculated by dividing income or loss attributable to common stockholders by the weighted average number of shares of common stock outstanding, excluding participating shares in accordance with ASC 260. To calculate diluted EPS, basic EPS is adjusted to include the effect of potentially dilutive stock options outstanding. The table below shows our basic and diluted EPS calculations.

|                                                                                         | Three Months Ended<br>March 31,<br>2019      2018<br>(Dollars in thousands,<br>except per<br>share amounts) |            |
|-----------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------|------------|
| <b>Numerator</b>                                                                        |                                                                                                             |            |
| Net income                                                                              | \$40,550                                                                                                    | \$38,764   |
| Less: distributed earnings allocated to participating securities                        | (111 )                                                                                                      | (105 )     |
| Less: undistributed earnings allocated to participating securities                      | (139 )                                                                                                      | (124 )     |
| Net income attributable to common stockholders (numerator for basic earnings per share) | 40,300                                                                                                      | 38,535     |
| Add back: undistributed earnings allocated to participating securities                  | 139                                                                                                         | 124        |
| Less: undistributed earnings reallocated to participating securities                    | (136 )                                                                                                      | (122 )     |
| Numerator for diluted earnings per share under two class method                         | \$40,303                                                                                                    | \$38,537   |
| <b>Denominator</b>                                                                      |                                                                                                             |            |
| Weighted-average common shares outstanding                                              | 60,939,364                                                                                                  | 60,340,774 |
| Add: dilutive effect of stock options                                                   | 1,217,846                                                                                                   | 1,106,789  |
| Add: dilutive effect of performance stock units                                         | 551,124                                                                                                     | -          |
| Denominator for diluted earnings per share under two class method                       | 62,708,334                                                                                                  | 61,447,563 |
| Basic Earnings Per Common Share                                                         | \$0.66                                                                                                      | \$0.64     |
| Diluted Earnings Per Common Share                                                       | \$0.64                                                                                                      | \$0.63     |

Diluted EPS for the three months ended March 31, 2019 and 2018 excluded options to purchase approximately 0.5 and 0.1 million shares of common stock, respectively, because the effect of their inclusion would be anti-dilutive.



Table of Contents**5. Accumulated Other Comprehensive Income**

The following table sets forth our changes in accumulated other comprehensive income (“AOCI”):

|                                  | Three<br>Months<br>Ended<br>March 31,<br>2018<br>(Dollars in<br>thousands) |
|----------------------------------|----------------------------------------------------------------------------|
| Beginning balance <sup>1</sup>   | \$- \$3,992                                                                |
| Adoption of accounting standards | - (3,992)                                                                  |
| Ending balance                   | \$- \$-                                                                    |

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<sup>(1)</sup> Amounts net-of-tax.

During the first quarter of 2018, an election was made to reclassify the income tax effects of the Tax Cuts and Jobs Act related to net unrealized gains on equity investments from accumulated other comprehensive income to retained earnings.

**6. Fair Value Measurements**

ASC Topic 820, *Fair Value Measurements* (“ASC 820”), defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. ASC 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs, other than quoted prices in active markets, that are either directly or indirectly observable; and Level 3, defined as unobservable inputs for which little or no market data exists, therefore requiring an entity to develop its own assumptions.

The following table sets forth the fair values and methods used for measuring the fair values of financial instruments on a recurring basis:

| Financial Instrument | Fair Value<br>Hierarchy |
|----------------------|-------------------------|
|----------------------|-------------------------|

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|                                      |         | March<br>31,              | December<br>31, |
|--------------------------------------|---------|---------------------------|-----------------|
|                                      |         | 2019                      | 2018            |
|                                      |         | (Dollars in<br>thousands) |                 |
| Cash and cash equivalents            |         |                           |                 |
| Debt securities (available-for-sale) | Level 1 | \$34,860                  | \$34,866        |
| Marketable securities                |         |                           |                 |
| Equity securities                    | Level 1 | \$45,767                  | \$40,879        |
| Mortgage loans held-for-sale, net    | Level 2 | \$110,810                 | \$149,211       |

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The following methods and assumptions were used to estimate the fair value of each class of financial instruments as of March 31, 2019 and December 31, 2018.

*Cash and cash equivalents (excluding debt securities with an original maturity of three months or less), restricted cash, trade and other receivables, prepaid and other assets, accounts payable, accrued liabilities and borrowings on our revolving credit facility.* Fair value approximates carrying value.

*Equity securities.* Our equity securities consist of holdings in common stock and exchange traded funds. As of March 31, 2019 and December 31, 2018, all of our equity securities were recorded at fair value with all changes in fair value recorded to net gain (loss) on marketable equity securities in the financial services section of our consolidated statements of operations and comprehensive income.

*Debt securities.* Our debt securities consist of U.S. government securities. As of March 31, 2019 and December 31, 2018, all of our debt securities were treated as available-for-sale investments and, as such, are recorded at fair value with all changes in fair value initially recorded through AOCI, subject to an assessment to determine if any unrealized loss, if applicable, is other-than-temporary.

The following tables set forth the cost and estimated fair value of our available for sale debt securities:

|                           | March 31, 2019         |      |               |          |
|---------------------------|------------------------|------|---------------|----------|
|                           | Amortized              | OTTI | Net Amortized | Fair     |
|                           | Cost                   |      | Cost          | Value    |
|                           | Basis                  |      | Cost          |          |
|                           | (Dollars in thousands) |      |               |          |
| <b>Financial Services</b> |                        |      |               |          |
| Cash and cash equivalents |                        |      |               |          |
| Debt securities           | \$34,860               | \$ - | \$ 34,860     | \$34,860 |

|                           | December 31, 2018 |      |               |          |
|---------------------------|-------------------|------|---------------|----------|
|                           | Amortized         | OTTI | Net Amortized | Fair     |
|                           | Cost              |      | Cost          | Value    |
|                           | Basis             |      | Cost          |          |
| <b>Financial Services</b> |                   |      |               |          |
| Cash and cash equivalents |                   |      |               |          |
| Debt securities           | \$34,866          | \$ - | \$ 34,866     | \$34,866 |





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The following table reconciles the net gain (loss) recognized during the three months ended March 31, 2019 and 2018 on equity securities to the unrealized gain (loss) recognized during the periods on equity securities still held at the reporting date.

|                                                                                                                     | Three Months<br>Ended<br>March 31,<br>2019    2018 |           |
|---------------------------------------------------------------------------------------------------------------------|----------------------------------------------------|-----------|
| Net gain (loss) recognized during the period on equity securities                                                   | \$4,840                                            | \$(1,153) |
| Less: Net gain recognized during the period on equity securities sold during the period                             | (237 )                                             | (96 )     |
| Unrealized gain (loss) recognized during the reporting period on equity securities still held at the reporting date | \$4,603                                            | \$(1,057) |

*Mortgage loans held-for-sale, net.* Our mortgage loans held-for-sale, which are measured at fair value on a recurring basis, include (1) mortgage loans held-for-sale that are under commitments to sell and (2) mortgage loans held-for-sale that are not under commitments to sell. At March 31, 2019 and December 31, 2018, we had \$96.2 million and \$130.8 million, respectively, of mortgage loans held-for-sale under commitments to sell. The fair value for those loans was based on quoted market prices for those mortgage loans, which are Level 2 fair value inputs. At March 31, 2019 and December 31, 2018, we had \$14.6 million and \$18.5 million, respectively, of mortgage loans held-for-sale that were not under commitments to sell. The fair value for those loans was primarily based upon the estimated market price received from an outside party, which is a Level 2 fair value input.

Gains on sales of mortgage loans, net, are included as a component of revenues in the financial services section of our consolidated statements of operations and comprehensive income. For the three months ended March 31, 2019, we recorded net gains on the sales of mortgage loans of \$11.7 million, compared to \$9.0 million for the same period in the prior year.

*Mortgage Repurchase Facility.* The debt associated with our mortgage repurchase facility (see Note 19 for further discussion) is at floating rates that approximate current market rates and have relatively short-term maturities, generally within 30 days. The fair value approximates carrying value and is based on Level 2 inputs.

*Senior Notes.* The estimated values of the senior notes in the following table are based on Level 2 inputs, which primarily reflect estimated prices for our senior notes which were provided by multiple sources.

March 31, 2019

December 31, 2018

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|                                                       | Carrying<br>Amount     | Fair<br>Value | Carrying<br>Amount | Fair<br>Value |
|-------------------------------------------------------|------------------------|---------------|--------------------|---------------|
|                                                       | (Dollars in thousands) |               |                    |               |
| \$250 Million 5 % Senior Notes due February 2020, net | \$249,109              | \$254,304     | \$248,850          | \$253,413     |
| \$250 Million 5½% Senior Notes due January 2024, net  | 248,841                | 258,479       | 248,789            | 242,983       |
| \$500 Million 6% Senior Notes due January 2043, net   | 490,372                | 434,117       | 490,328            | 386,552       |
| Total                                                 | \$988,322              | \$946,900     | \$987,967          | \$882,948     |

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Table of Contents**7. Inventories**

The following table sets forth, by reportable segment, information relating to our homebuilding inventories:

|                                          | March 31,<br>2019      | December<br>31,<br>2018 |
|------------------------------------------|------------------------|-------------------------|
|                                          | (Dollars in thousands) |                         |
| Housing completed or under construction: |                        |                         |
| West                                     | \$516,900              | \$521,960               |
| Mountain                                 | 356,177                | 347,738                 |
| East                                     | 77,197                 | 82,738                  |
| Subtotal                                 | 950,274                | 952,436                 |
| Land and land under development:         |                        |                         |
| West                                     | 699,704                | 705,591                 |
| Mountain                                 | 420,155                | 402,657                 |
| East                                     | 78,965                 | 72,310                  |
| Subtotal                                 | 1,198,824              | 1,180,558               |
| Total inventories                        | \$2,149,098            | \$2,132,994             |

Our inventories are primarily associated with communities where we intend to construct and sell homes, including models and unsold homes. Costs capitalized to land and land under development primarily include: (1) land costs; (2) land development costs; (3) entitlement costs; (4) capitalized interest; (5) engineering fees; and (6) title insurance, real property taxes and closing costs directly related to the purchase of the land parcel. Components of housing completed or under construction primarily include: (1) land costs transferred from land and land under development; (2) direct construction costs associated with a house; (3) real property taxes, engineering fees, permits and other fees; (4) capitalized interest; and (5) indirect construction costs, which include field construction management salaries and benefits, utilities and other construction related costs. Land costs are transferred from land and land under development to housing completed or under construction at the point in time that construction of a home on an owned lot begins.

In accordance with ASC Topic 360, *Property, Plant, and Equipment* (“ASC 360”), homebuilding inventories, excluding those classified as held for sale, are carried at cost unless events and circumstances indicate that the carrying value of the underlying subdivision may not be recoverable. We evaluate inventories for impairment at each quarter end on a subdivision level basis as each such subdivision represents the lowest level of identifiable cash flows. In making this determination, we review, among other things, the following for each subdivision:

• actual and trending “Operating Margin” (which is defined as home sale revenues less home cost of sales and all incremental costs associated directly with the subdivision, including sales commissions and marketing costs);

- estimated future undiscounted cash flows and Operating Margin;
- forecasted Operating Margin for homes in backlog;
- actual and trending net home orders;
  - homes available for sale;
- market information for each sub-market, including competition levels, home foreclosure levels, the size and style of homes currently being offered for sale and lot size; and
- known or probable events indicating that the carrying value may not be recoverable.

If events or circumstances indicate that the carrying value of our inventory may not be recoverable, assets are reviewed for impairment by comparing the undiscounted estimated future cash flows from an individual subdivision (including capitalized interest) to its carrying value. If the undiscounted future cash flows are less than the subdivision's carrying value, the carrying value of the subdivision is written down to its then estimated fair value. We generally determine the estimated fair value of each subdivision by determining the present value of the estimated future cash flows at discount rates, which are Level 3 inputs, that are commensurate with the risk of the subdivision under evaluation. The evaluation for the recoverability of the carrying value of the assets for each individual subdivision can be impacted significantly by our estimates of future home sale revenues, home construction costs, and development costs per home, all of which are Level 3 inputs.

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If land is classified as held for sale, we measure it in accordance with ASC 360 at the lower of the carrying value or fair value less estimated costs to sell. In determining fair value, we primarily rely upon the most recent negotiated price which is a Level 2 input. If a negotiated price is not available, we will consider several factors including, but not limited to, current market conditions, recent comparable sales transactions and market analysis studies, which are considered Level 3 inputs. If the fair value less estimated costs to sell is lower than the current carrying value, the land is impaired down to its estimated fair value less costs to sell.

Impairments of homebuilding inventory by segment for the three months ended March 31, 2019 and 2018 are shown in the table below.

|                             | Three<br>Months<br>Ended<br>March 31,<br>2019 2018<br>(Dollars in<br>thousands) |       |
|-----------------------------|---------------------------------------------------------------------------------|-------|
| West                        | \$-                                                                             | \$375 |
| Mountain                    | 400                                                                             | 175   |
| East                        | 210                                                                             | -     |
| Total inventory impairments | \$610                                                                           | \$550 |

The table below provides quantitative data, for the periods presented, used in determining the fair value of the impaired inventory.

| Three Months Ended | Impairment Data           |                       |                                           | Quantitative Data               |               |
|--------------------|---------------------------|-----------------------|-------------------------------------------|---------------------------------|---------------|
|                    | Total Subdivisions Tested | Inventory Impairments | Fair Value of Inventory After Impairments | Number of Subdivisions Impaired | Discount Rate |
|                    | (Dollars in thousands)    |                       |                                           |                                 |               |
| March 31, 2019     | 16                        | \$ 610                | \$ 10,476                                 | 2                               | N/A           |
| March 31, 2018     | 24                        | \$ 550                | \$ 5,223                                  | 2                               | 12 %          |

**8. Capitalization of Interest**

We capitalize interest to inventories during the period of development in accordance with ASC Topic 835, *Interest* (“ASC 835”). Homebuilding interest capitalized as a cost of inventories is included in cost of sales during the period that related units or lots are delivered. To the extent our homebuilding debt exceeds our qualified assets as defined in ASC 835, we expense a portion of the interest incurred. Qualified homebuilding assets consist of all lots and homes, excluding finished unsold homes or finished models, within projects that are actively selling or under development. The table set forth below summarizes homebuilding interest activity. For all periods presented below, our qualified assets exceeded our homebuilding debt and as such, all interest incurred has been capitalized.

|                                                                               | Three Months<br>Ended<br>March 31, |          |
|-------------------------------------------------------------------------------|------------------------------------|----------|
|                                                                               | 2019                               | 2018     |
|                                                                               | (Dollars in<br>thousands)          |          |
| Homebuilding interest incurred                                                | \$16,031                           | \$15,625 |
| Less: Interest capitalized                                                    | (16,031)                           | (15,625) |
| Homebuilding interest expensed                                                | \$-                                | \$-      |
| Interest capitalized, beginning of period                                     | \$54,845                           | \$57,541 |
| Plus: Interest capitalized during period                                      | 16,031                             | 15,625   |
| Less: Previously capitalized interest included in home and land cost of sales | (13,929)                           | (14,428) |
| Interest capitalized, end of period                                           | \$56,947                           | \$58,738 |

Table of Contents**9. Leases**

We lease certain property, land and equipment, the majority of which comprise property related leases to provide office space where we operate our business. Leases with an initial term of 12 months or less are not recorded on the balance sheet. We recognize lease expense for these leases on a straight-line basis over the lease term.

Our property related leases typically have terms of between three and five years, with the exception of the lease governing the Company's headquarters, and are classified as operating leases. These leases do not contain any residual value guarantees or restrictive covenants and no variable lease payments, except for common area maintenance and real estate taxes. Many of our property related leases give us the option to extend the lease term for a period of time, generally consistent with the initial lease term. These options are excluded from our calculation of the right-of-use asset and lease liability until such time as we determine it is reasonably certain that the option will be exercised.

The property related lease for the Company's headquarters in Denver, Colorado is ten years in length with an expiration date of October 31, 2026 and contains a ten year option to extend the term of the lease through 2036. This option has been excluded from our calculation of the right-of-use asset and lease liability as it is not currently considered reasonably certain that the option will be exercised.

Operating lease expense is included as a component of selling, general and administrative expenses and expenses in the homebuilding and financial services sections of our consolidated statements of operations and comprehensive income, respectively. Components of operating lease expense were as follows:

|                                   |                                                                            |
|-----------------------------------|----------------------------------------------------------------------------|
|                                   | Three<br>Months<br>Ended<br>March 31,<br>2019<br>(Dollars in<br>thousands) |
| Operating lease cost <sup>1</sup> | \$ 1,980                                                                   |
| Less: Sublease income (Note 20)   | (37 )                                                                      |
| Net lease cost                    | \$ 1,943                                                                   |

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<sup>1</sup> Includes variable lease costs, which are immaterial.

Supplemental cash flow information related to leases was as follows:



|                                                                         | Three<br>Months<br>Ended<br>March 31,<br>2019<br>(Dollars in<br>thousands) |
|-------------------------------------------------------------------------|----------------------------------------------------------------------------|
| Cash paid for amounts included in the measurement of lease liabilities: |                                                                            |
| Operating cash flows from operating leases                              | \$ 1,771                                                                   |
| Leased assets obtained in exchange for new operating lease liabilities  | \$ 1,477                                                                   |

Supplemental cash flow information related to non-cash transactions also includes the recognition of operating lease right-of-use assets of \$33.5 million and operating lease liabilities of \$34.3 million upon adoption of ASC 842.

Weighted-average remaining lease term and discount rate for operating leases were as follows:

|                                                  | March<br>31,<br>2019 |
|--------------------------------------------------|----------------------|
| Weighted-average remaining lease term (in years) | 6.8                  |
| Weighted-average discount rate                   | 5.5 %                |

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Maturities of operating lease liabilities were as follows:

|                                                           | Year<br>Ended<br>December<br>31,<br>(Dollars in<br>thousands) |
|-----------------------------------------------------------|---------------------------------------------------------------|
| 2019 (excluding the three months ended March 31, 2019)    | \$ 5,315                                                      |
| 2020                                                      | 6,317                                                         |
| 2021                                                      | 6,066                                                         |
| 2022                                                      | 5,752                                                         |
| 2023                                                      | 5,148                                                         |
| Thereafter                                                | 13,118                                                        |
| Total operating lease payments <sup>1</sup>               | \$ 41,716                                                     |
| Less: Interest                                            | 7,133                                                         |
| Present value of operating lease liabilities <sup>2</sup> | \$ 34,583                                                     |

<sup>1</sup> Operating lease payments exclude \$0.6 million of legally binding lease payments for leases signed but not yet commenced.

<sup>2</sup> Financial services operating lease liabilities of \$1.1 million are included as a component of accrued liabilities in the financial services section of our consolidated balance sheet at March 31, 2019.

**10. Homebuilding Prepaid and Other Assets**

The following table sets forth the components of homebuilding prepaid and other assets:

|                                                                | March<br>31,<br>2019      | December<br>31,<br>2018 |
|----------------------------------------------------------------|---------------------------|-------------------------|
|                                                                | (Dollars in<br>thousands) |                         |
| Land option deposits                                           | \$21,951                  | \$ 23,805               |
| Goodwill                                                       | 6,008                     | 6,008                   |
| Prepaid expenses                                               | 6,614                     | 7,324                   |
| Deferred debt issuance costs on revolving credit facility, net | 7,279                     | 7,662                   |
| Other                                                          | 693                       | 995                     |
| Total                                                          | \$42,545                  | \$ 45,794               |

**11. Homebuilding Accrued Liabilities and Financial Services Accounts Payable and Accrued Liabilities**

The following table sets forth information relating to homebuilding accrued liabilities:

|                                                 | March<br>31,<br>2019      | December<br>31,<br>2018 |
|-------------------------------------------------|---------------------------|-------------------------|
|                                                 | (Dollars in<br>thousands) |                         |
| Customer and escrow deposits                    | \$36,986                  | \$34,463                |
| Warranty accrual                                | 29,992                    | 28,262                  |
| Accrued compensation and related expenses       | 22,438                    | 39,459                  |
| Accrued interest                                | 13,281                    | 27,734                  |
| Construction defect claim reserves              | 8,367                     | 8,464                   |
| Land development and home construction accruals | 9,064                     | 8,683                   |
| Income taxes payable                            | 18,337                    | 6,245                   |
| Other accrued liabilities                       | 46,666                    | 42,937                  |
| Total accrued liabilities                       | \$185,131                 | \$196,247               |

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The following table sets forth information relating to financial services accounts payable and accrued liabilities:

|                                                | March<br>31,<br>2019      | December<br>31,<br>2018 |
|------------------------------------------------|---------------------------|-------------------------|
|                                                | (Dollars in<br>thousands) |                         |
| Insurance reserves                             | \$47,852                  | \$ 46,844               |
| Accounts payable and other accrued liabilities | 11,022                    | 11,699                  |
| Total accounts payable and accrued liabilities | \$58,874                  | \$ 58,543               |

**12. Warranty Accrual**

Our homes are sold with limited third-party warranties and, under our agreement with the issuer of the third-party warranties, we are responsible for performing all of the work for the first two years of the warranty coverage and paying for substantially all of the work required to be performed during years three through ten of the warranties. We record accruals for general and structural warranty claims, as well as accruals for known, unusual warranty-related expenditures. Our warranty accrual is recorded based upon historical payment experience in an amount estimated to be adequate to cover expected costs of materials and outside labor during warranty periods. The determination of the warranty accrual rate for closed homes and the evaluation of our warranty accrual balance at period end are based on an internally developed analysis that includes known facts and interpretations of circumstances, including, among other things, our trends in historical warranty payment levels and warranty payments for claims not considered to be normal and recurring.

Our warranty accrual is included in accrued liabilities in the homebuilding section of our consolidated balance sheets and adjustments to our warranty accrual are recorded as an increase or reduction to home cost of sales in the homebuilding section of our consolidated statements of operations and comprehensive income.

The table set forth below summarizes accrual, adjustment and payment activity related to our warranty accrual for the three months ended March 31, 2019 and 2018. For the three months ended March 31, 2019 and 2018, we recorded adjustments to increase our warranty accrual by \$0.9 million and \$3.1 million, respectively. The adjustments recorded during the three months ended March 31, 2019 related to homes with structural related issues, while the adjustments recorded during the three months ended March 31, 2018 were due to higher than expected general warranty related expenditures.

Three Months  
Ended

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March 31,  
2019 2018  
(Dollars in  
thousands)

|                                |          |          |
|--------------------------------|----------|----------|
| Balance at beginning of period | \$28,262 | \$21,909 |
| Expense provisions             | 3,348    | 2,598    |
| Cash payments                  | (2,493 ) | (2,500 ) |
| Adjustments                    | 875      | 3,106    |
| Balance at end of period       | \$29,992 | \$25,113 |

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Table of Contents**13. Insurance and Construction Defect Claim Reserves**

The establishment of reserves for estimated losses associated with insurance policies issued by Allegiant and re-insurance agreements issued by StarAmerican are based on actuarial studies that include known facts and interpretations of circumstances, including our experience with similar cases and historical trends involving claim payment patterns, pending levels of unpaid claims, product mix or concentration, claim severity, frequency patterns depending on the business conducted, and changing regulatory and legal environments. It is possible that changes in the insurance payment experience used in estimating our ultimate insurance losses could have a material impact on our insurance reserves.

The establishment of reserves for estimated losses to be incurred by our homebuilding subsidiaries associated with (1) the self-insured retention (“SIR”) portion of construction defect claims that are expected to be covered under insurance policies with Allegiant and (2) the entire cost of any construction defect claims that are not expected to be covered by insurance policies with Allegiant are based on actuarial studies that include known facts similar to those established for our insurance reserves. It is possible that changes in the payment experience used in estimating our ultimate losses for construction defect claims could have a material impact on our reserves.

The table set forth below summarizes our insurance and construction defect claim reserves activity for the three months ended March 31, 2019 and 2018. These reserves are included as a component of accrued liabilities in the financial services and homebuilding sections of the consolidated balance sheets.

|                                  | Three Months<br>Ended<br>March 31,<br>2019      2018<br>(Dollars in<br>thousands) |          |
|----------------------------------|-----------------------------------------------------------------------------------|----------|
| Balance at beginning of period   | \$55,308                                                                          | \$52,686 |
| Expense provisions               | 2,465                                                                             | 2,304    |
| Cash payments, net of recoveries | (1,554 )                                                                          | (1,595 ) |
| Balance at end of period         | \$56,219                                                                          | \$53,395 |

In the ordinary course of business, we make payments from our insurance and construction defect claim reserves to settle litigation claims arising from our homebuilding activities. These payments are irregular in both their timing and their magnitude. As a result, the cash payments, net of recoveries shown for the three months ended March 31, 2019 and 2018 are not necessarily indicative of what future cash payments will be for subsequent periods.

## 14. Income Taxes

Our overall effective income tax rates were 27.1% and 23.3% for the three months ended March 31, 2019 and 2018, respectively, resulting in income tax expense of \$15.1 million and \$11.8 million for the same periods, respectively. The year-over-year increase in our effective tax rate for the three months ended March 31, 2019 was due to a \$1.2 million benefit from energy tax credits which reduced our 2018 first quarter tax rate. It is currently uncertain as to the extent, if any, that energy tax credits will impact our 2019 results, and therefore no benefit was recorded for the 2019 first quarter.

At March 31, 2019 and December 31, 2018 we had deferred tax assets, net of valuation allowances and deferred tax liabilities, of \$34.5 million and \$37.2 million, respectively. The valuation allowances were primarily related to various state net operating loss carryforwards where realization is more uncertain at this time due to the limited carryforward periods coupled with minimal operating activity that exists in certain states.

Table of Contents**15. Senior Notes**

The carrying value of our senior notes as of March 31, 2019 and December 31, 2018, net of any unamortized debt issuance costs or discount, were as follows:

|                                         | March<br>31,<br>2019      | December<br>31,<br>2018 |
|-----------------------------------------|---------------------------|-------------------------|
|                                         | (Dollars in<br>thousands) |                         |
| 5 % Senior Notes due February 2020, net | \$249,109                 | \$248,850               |
| 5½% Senior Notes due January 2024, net  | 248,841                   | 248,789                 |
| 6% Senior Notes due January 2043, net   | 490,372                   | 490,328                 |
| Total                                   | \$988,322                 | \$987,967               |

Our senior notes are not secured and, while the senior note indentures contain some restrictions on secured debt and other transactions, they do not contain financial covenants. Our senior notes are fully and unconditionally guaranteed on an unsecured basis, jointly and severally, by most of our homebuilding segment subsidiaries.

**16. Stock-Based Compensation**

We account for share-based awards in accordance with ASC Topic 718 *Compensation—Stock Compensation* (“ASC 718”), which requires the fair value of stock-based compensation awards to be amortized as an expense over the vesting period. Stock-based compensation awards are valued at fair value on the date of grant. The following table sets forth share-based award expense activity for the three months ended March 31, 2019 and 2018:

|                                 | Three Months<br>Ended<br>March 31,<br>2019 2018 |         |
|---------------------------------|-------------------------------------------------|---------|
|                                 | (Dollars in<br>thousands)                       |         |
| Stock option grants expense     | \$255                                           | \$56    |
| Restricted stock awards expense | 911                                             | 744     |
| Performance share units expense | 3,085                                           | 451     |
| Total stock based compensation  | \$4,251                                         | \$1,251 |





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On May 23, 2018, June 20, 2017 and July 25, 2016, the Company granted long term performance stock unit awards (“PSUs”) to each of the CEO, the COO, and the Chief Financial Officer (“CFO”) under the Company’s 2011 Equity Incentive Plan. The PSUs will be earned based upon the Company’s performance, over a three year period (the “Performance Period”), measured by increasing home sale revenues over a “Base Period.” Each award is conditioned upon the Company achieving an average gross margin from home sales (excluding impairments) of at least fifteen percent (15%) over the Performance Period. Target goals will be earned if the Company’s three year average home sale revenues over the Performance Period (“Performance Revenues”) exceed the home sale revenues over the Base Period (“Base Revenues”) by at least 10% but less than 20%. If Performance Revenues exceed the Base Revenues by at least 5% but less than 10%, 50% of the Target Goals will be earned (“Threshold Goals”). If Performance Revenues exceed the Base Revenues by at least 20%, 200% of the Target Goals will be earned (“Maximum Goals”). For the PSUs granted in 2017 and 2018, the number of PSUs earned shall be adjusted to be proportional to the partial performance between the Threshold Goals, Target Goals and Maximum Goals. Details for each defined term above for each grant has been provided in the table below.

| Awardee | Date of Award | Performance Period | Base Period    | Threshold Goal       |                    | Target Goal     |                    | Maximum Goal    |                    |                 |
|---------|---------------|--------------------|----------------|----------------------|--------------------|-----------------|--------------------|-----------------|--------------------|-----------------|
|         |               |                    |                | Base Period Revenues | Home Sale Revenues | PSUs            | Home Sale Revenues | PSUs            | Home Sale Revenues | PSUs            |
| CEO     | July 25, 2016 | July 1, 2016       | July 1, 2015   |                      |                    | 61,236          |                    | 122,472         |                    | 244,944         |
| COO     |               | to                 | to             | \$1.975 billion      | 61,236             | \$2.074 billion | 122,472            | \$2.173 billion | 244,944            | \$2.370 billion |
| CFO     |               | June 30, 2019      | June 30, 2016  |                      | 15,309             |                 | 30,618             |                 | 61,236             |                 |
| CEO     | June 20, 2017 | April 1, 2017      | April 1, 2016  |                      |                    | 64,152          |                    | 128,304         |                    | 256,608         |
| COO     |               | to                 | to             | \$2.426 billion      | 64,152             | \$2.547 billion | 128,304            | \$2.669 billion | 256,608            | \$2.911 billion |
| CFO     |               | March 31, 2020     | March 31, 2017 |                      | 16,038             |                 | 32,076             |                 | 64,152             |                 |
| CEO     | May 23, 2018  | April 1, 2018      | April 1, 2017  |                      |                    | 64,800          |                    | 129,600         |                    | 259,200         |
| COO     |               | to                 | to             | \$2.543 billion      | 64,800             | \$2.670 billion | 129,600            | \$2.797 billion | 259,200            | \$3.052 billion |
| CFO     |               | March 31, 2021     | March 31, 2018 |                      | 16,200             |                 | 32,400             |                 | 64,800             |                 |

\* Dollars in thousands

In accordance with ASC 718, the PSUs were valued on the date of grant at their fair value. The fair value of these grants was equal to the closing price of MDC stock on the date of grant less the discounted cash flows of expected future dividends over the respective vesting period (as these PSUs do not participate in dividends). The grant date fair value and maximum potential expense if the Maximum Goals were met for these awards has been provided in the table above. ASC 718 does not permit recognition of expense associated with performance-based stock awards until achievement of the performance targets are probable of occurring.

*2016 PSU Grants.* As of March 31, 2019, the Company determined that achievement of the Maximum Goals for these awards was probable and as such, the Company recorded share-based award expense related to the awards of \$0.9 million for the three months ended March 31, 2019. As of March 31, 2018, the Company had concluded that achievement of the Target Goals was probable and, as such, recorded share-based award expense related to the awards of \$0.5 million for the three months ended March 31, 2018.

*2017 PSU Grants.* As of March 31, 2019, the Company determined that achievement of the Target Goals for these awards was probable and as such, the Company recorded share-based award expense related to the awards of \$2.2 million for the three months ended March 31, 2019. As of March 31, 2018, the Company concluded that achievement of any of the performance metrics had not met the level of probability required to record compensation expense and as such, no expense related to the grant of these awards had been recognized as of March 31, 2018.

*2018 PSU Grants.* For the PSUs granted in May of 2018, the Company concluded that achievement of any of the performance metrics has not met the level of probability required to record compensation expense and, as such, no expense related to these awards has been recognized as of March 31, 2019.

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**17. Commitments and Contingencies**

*Surety Bonds and Letters of Credit.* We are required to obtain surety bonds and letters of credit in support of our obligations for land development and subdivision improvements, homeowner association dues, warranty work, contractor license fees and earnest money deposits. At March 31, 2019, we had outstanding surety bonds and letters of credit totaling \$245.5 million and \$89.3 million, respectively, including \$61.7 million in letters of credit issued by HomeAmerican. The estimated cost to complete obligations related to these bonds and letters of credit were approximately \$126.6 million and \$51.2 million, respectively. All letters of credit as of March 31, 2019, excluding those issued by HomeAmerican, were issued under our unsecured revolving credit facility (see Note 19 for further discussion of the revolving credit facility). We expect that the obligations secured by these performance bonds and letters of credit generally will be performed in the ordinary course of business and in accordance with the applicable contractual terms. To the extent that the obligations are performed, the related performance bonds and letters of credit should be released and we should not have any continuing obligations. However, in the event any such performance bonds or letters of credit are called, our indemnity obligations could require us to reimburse the issuer of the performance bond or letter of credit.

We have made no material guarantees with respect to third-party obligations.

*Litigation.* Due to the nature of the homebuilding business, we have been named as defendants in various claims, complaints and other legal actions arising in the ordinary course of business, including product liability claims and claims associated with the sale and financing of homes. In the opinion of management, the outcome of these ordinary course matters will not have a material adverse effect upon our financial condition, results of operations or cash flows.

*Lot Option Contracts.* In the ordinary course of business, we enter into lot option purchase contracts (“Option Contracts”), generally through a deposit of cash or a letter of credit, for the right to purchase land or lots at a future point in time with predetermined terms. The use of such land option and other contracts generally allow us to reduce the risks associated with direct land ownership and development, reduces our capital and financial commitments, and minimizes the amount of land inventories on our consolidated balance sheets. In certain cases, these contracts will be settled shortly following the end of the period. Our obligation with respect to Option Contracts is generally limited to forfeiture of the related deposits. At March 31, 2019, we had cash deposits and letters of credit totaling \$19.3 million and \$4.8 million, respectively, at risk associated with the option to purchase 6,368 lots.

**18. Derivative Financial Instruments**

The derivative instruments we utilize in the normal course of business are interest rate lock commitments and forward sales of mortgage-backed securities, both of which typically are short-term in nature. Forward sales of

mortgage-backed securities are utilized to hedge changes in fair value of our interest rate lock commitments as well as mortgage loans held-for-sale not under commitments to sell. For forward sales of mortgage-backed securities, as well as interest rate lock commitments that are still outstanding at the end of a reporting period, we record the changes in fair value of the derivatives in revenues in the financial services section of our consolidated statements of operations and comprehensive income with an offset to other assets or accounts payable and accrued liabilities in the financial services section of our consolidated balance sheets, depending on the nature of the change.

At March 31, 2019, we had interest rate lock commitments with an aggregate principal balance of \$149.4 million. Additionally, we had \$14.1 million of mortgage loans held-for-sale at March 31, 2019 that had not yet been committed to a mortgage purchaser. In order to hedge the changes in fair value of our interest rate lock commitments and mortgage loans held-for-sale that had not yet been committed to a mortgage purchaser, we had forward sales of securities totaling \$121.0 million at March 31, 2019.

For the three months ended March 31, 2019 and 2018, we recorded net gains of \$0.9 million and \$1.5 million, respectively, on our derivatives.

Table of Contents**19. Lines of Credit**

*Revolving Credit Facility.* We have an unsecured revolving credit agreement (“Revolving Credit Facility”) with a group of lenders which may be used for general corporate purposes. This agreement was amended on November 1, 2018 to (1) extend the Revolving Credit Facility maturity to December 18, 2023, (2) increase the aggregate commitment from \$700 million to \$1.0 billion (the “Commitment”) and (3) provide that the aggregate amount of the commitments may increase to an amount not to exceed \$1.5 billion upon our request, subject to receipt of additional commitments from existing or additional lenders and, in the case of additional lenders, the consent of the co-administrative agents. As defined in the Revolving Credit Facility, interest rates on base rate borrowings are equal to the highest of (1) 0.0%, (2) a prime rate, (3) a federal funds effective rate plus 1.50%, and (4) a specified eurocurrency rate plus 1.00% and, in each case, plus a margin that is determined based on our credit ratings and leverage ratio. Interest rates on eurocurrency borrowings are equal to a specified eurocurrency rate plus a margin that is determined based on our credit ratings and leverage ratio. At any time at which our leverage ratio, as of the last day of the most recent calendar quarter, exceeds 55%, the aggregate principal amount of all consolidated senior debt borrowings outstanding may not exceed the borrowing base. There is no borrowing base requirement if our leverage ratio, as of the last day of the most recent calendar quarter, is 55% or less.

The Revolving Credit Facility is fully and unconditionally guaranteed, jointly and severally, by most of our homebuilding segment subsidiaries. The facility contains various representations, warranties and covenants that we believe are customary for agreements of this type. The financial covenants include a consolidated tangible net worth test and a leverage test, along with a consolidated tangible net worth covenant, all as defined in the Revolving Credit Facility. A failure to satisfy the foregoing tests does not constitute an event of default, but can trigger a “term-out” of the facility. A breach of the consolidated tangible net worth covenant (but not the consolidated tangible net worth test) or a violation of anti-corruption or sanctions laws would result in an event of default.

The Revolving Credit Facility is subject to acceleration upon certain specified events of default, including breach of the consolidated tangible net worth covenant, a violation of anti-corruption or sanctions laws, failure to make timely payments, breaches of certain representations or covenants, failure to pay other material indebtedness, or another person becoming beneficial owner of 50% or more of our outstanding common stock. We believe we were in compliance with the representations, warranties and covenants included in the Revolving Credit Facility as of March 31, 2019.

We incur costs associated with unused commitment fees pursuant to the terms of the Revolving Credit Facility. At March 31, 2019 and December 31, 2018, there were \$27.6 million and \$27.8 million, respectively, in letters of credit outstanding, which reduced the amounts available to be borrowed under the Revolving Credit Facility. We had \$15.0 million outstanding under the Revolving Credit Facility as of March 31, 2019 and December 31, 2018. As of March 31, 2019, availability under the Revolving Credit Facility was approximately \$957.4 million.

*Mortgage Repurchase Facility.* HomeAmerican has a Master Repurchase Agreement (the “Mortgage Repurchase Facility”) with U.S. Bank National Association (“USBNA”). Effective August 9, 2018, the Mortgage Repurchase Facility was amended to extend its termination date to August 8, 2019. The Mortgage Repurchase Facility provides liquidity to HomeAmerican by providing for the sale of up to an aggregate of \$75 million (subject to increase by up to \$75 million under certain conditions) of eligible mortgage loans to USBNA with an agreement by HomeAmerican to repurchase the mortgage loans at a future date. Until such mortgage loans are transferred back to HomeAmerican, the documents relating to such loans are held by USBNA, as custodian, pursuant to the Custody Agreement (“Custody Agreement”), dated as of November 12, 2008, by and between HomeAmerican and USBNA. In the event that an eligible mortgage loan becomes ineligible, as defined under the Mortgage Repurchase Facility, HomeAmerican may be required to repurchase the ineligible mortgage loan immediately. The maximum aggregate commitment of the Mortgage Repurchase Facility was temporarily increased on March 27, 2019 from \$75 million to \$100 million and was effective through April 24, 2019. The Mortgage Repurchase Facility also had a temporary increase in the maximum aggregate commitment from \$75 million to \$130 million on December 27, 2018 and was effective through January 25, 2019. At March 31, 2019 and December 31, 2018, HomeAmerican had \$84.9 million and \$116.8 million, respectively, of mortgage loans that HomeAmerican was obligated to repurchase under the Mortgage Repurchase Facility. Mortgage loans that HomeAmerican is obligated to repurchase under the Mortgage Repurchase Facility are accounted for as a debt financing arrangement and are reported as mortgage repurchase facility in the consolidated balance sheets. Advances under the Mortgage Repurchase Facility carry a price range that is based on a LIBOR rate or successor benchmark rate.

The Mortgage Repurchase Facility contains various representations, warranties and affirmative and negative covenants that we believe are customary for agreements of this type. The negative covenants include, among others, (i) a minimum Adjusted Tangible Net Worth requirement, (ii) a maximum Adjusted Tangible Net Worth ratio, (iii) a minimum adjusted net income requirement, and (iv) a minimum Liquidity requirement. The foregoing capitalized terms are defined in the Mortgage Repurchase Facility. We believe HomeAmerican was in compliance with the representations, warranties and covenants included in the Mortgage Repurchase Facility as of March 31, 2019.

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**20. Related Party Transactions**

We contributed \$0.5 million in cash to the MDC/Richmond American Homes Foundation (the "Foundation") during the three months ended March 31, 2019. The Foundation is a non-profit organization operated exclusively for charitable, educational and other purposes beneficial to social welfare within the meaning of Section 501(c)(3) of the Internal Revenue Code. The following Directors and/or officers of the Company served as directors of the Foundation at March 31, 2019, all of whom serve without compensation:

| Name               | MDC Title         |
|--------------------|-------------------|
| Larry A. Mizel     | Chairman and CEO  |
| David D. Mandarich | President and COO |

Three other individuals, who are independent of the Company, also serve as directors of the Foundation. All directors of the Foundation serve without compensation.

The Company has a sublease agreement with CVentures, Inc. Larry A. Mizel, the Chief Executive Officer of the Company, is the President of CVentures, Inc. The sublease is for office space that CVentures, Inc. has continuously leased from the Company since 2005. The current sublease term commenced November 1, 2016 and will continue through October 31, 2021, with an option to extend to October 31, 2026. The sublease agreement is for approximately 5,437 rentable square feet at a base rent that increases over the initial term from \$26.50 to \$28.68 per rentable square foot per year, and increasing over the extension term from \$29.26 to \$31.67 per rentable square foot per year. The sublease rent is an allocation of the rent under the master lease agreement based on the sublease square footage.

**21. Supplemental Guarantor Information**

Our senior notes are fully and unconditionally guaranteed on an unsecured basis, jointly and severally, by the following subsidiaries (collectively, the "Guarantor Subsidiaries"), which are 100%-owned subsidiaries of the Company:

- M.D.C. Land Corporation
- RAH of Florida, Inc.
- Richmond American Construction, Inc.
- Richmond American Homes of Arizona, Inc.
- Richmond American Homes of Colorado, Inc.
- Richmond American Homes of Florida, LP



Richmond American Homes of Illinois, Inc.  
Richmond American Homes of Maryland, Inc.  
Richmond American Homes of Nevada, Inc.  
Richmond American Homes of New Jersey, Inc.  
Richmond American Homes of Oregon, Inc.  
Richmond American Homes of Pennsylvania, Inc.  
Richmond American Homes of Utah, Inc.  
Richmond American Homes of Virginia, Inc.  
Richmond American Homes of Washington, Inc.

The senior note indentures do not provide for a suspension of the guarantees, but do provide that any Guarantor may be released from its guarantee so long as (1) no default or event of default exists or would result from release of such guarantee, (2) the Guarantor being released has consolidated net worth of less than 5% of the Company's consolidated net worth as of the end of the most recent fiscal quarter, (3) the Guarantors released from their guarantees in any year-end period comprise in the aggregate less than 10% (or 15% if and to the extent necessary to permit the cure of a default) of the Company's consolidated net worth as of the end of the most recent fiscal quarter, (4) such release would not have a material adverse effect on the homebuilding business of the Company and its subsidiaries and (5) the Guarantor is released from its guarantee(s) under all Specified Indebtedness (other than by reason of payment under its guarantee of Specified Indebtedness). Upon delivery of an officers' certificate and an opinion of counsel stating that all conditions precedent provided for in the indenture relating to such transactions have been complied with and the release is authorized, the guarantee will be automatically and unconditionally released. "Specified Indebtedness" means indebtedness under the senior notes, the Company's Indenture dated as of December 3, 2002, the Revolving Credit Facility, and any refinancing, extension, renewal or replacement of any of the foregoing.

We have determined that separate, full financial statements of the Guarantor Subsidiaries would not be material to investors and, accordingly, supplemental financial information for the Guarantor and Non-Guarantor Subsidiaries is presented below.

Table of Contents**Supplemental Condensed Combining Balance Sheet**

|                                                       | March 31, 2019         |                           |                                   |                        |                     |
|-------------------------------------------------------|------------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                                       | MDC                    | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|                                                       | (Dollars in thousands) |                           |                                   |                        |                     |
| <b>ASSETS</b>                                         |                        |                           |                                   |                        |                     |
| <b>Homebuilding:</b>                                  |                        |                           |                                   |                        |                     |
| Cash and cash equivalents                             | \$411,750              | \$4,624                   | \$ -                              | \$-                    | \$ 416,374          |
| Restricted cash                                       | -                      | 8,136                     | -                                 | -                      | 8,136               |
| Trade and other receivables                           | 589                    | 67,371                    | -                                 | -                      | 67,960              |
| Inventories:                                          |                        |                           |                                   |                        |                     |
| Housing completed or under construction               | -                      | 950,274                   | -                                 | -                      | 950,274             |
| Land and land under development                       | -                      | 1,198,824                 | -                                 | -                      | 1,198,824           |
| Total inventories                                     | -                      | 2,149,098                 | -                                 | -                      | 2,149,098           |
| Intercompany receivables                              | 1,939,500              | 6,509                     | -                                 | (1,946,009)            | -                   |
| Investment in subsidiaries                            | 272,420                | -                         | -                                 | (272,420)              | -                   |
| Property and equipment, net                           | 23,608                 | 36,157                    | -                                 | -                      | 59,765              |
| Operating lease right-of-use asset                    | 32,604                 | -                         | -                                 | -                      | 32,604              |
| Deferred tax asset, net                               | 34,513                 | -                         | -                                 | (9)                    | 34,504              |
| Prepaid and other assets                              | 11,050                 | 31,495                    | -                                 | -                      | 42,545              |
| Total homebuilding assets                             | 2,726,034              | 2,303,390                 | -                                 | (2,218,438)            | 2,810,986           |
| <b>Financial Services:</b>                            |                        |                           |                                   |                        |                     |
| Cash and cash equivalents                             | -                      | -                         | 51,556                            | -                      | 51,556              |
| Marketable securities                                 | -                      | -                         | 45,767                            | -                      | 45,767              |
| Intercompany receivables                              | -                      | -                         | 21,713                            | (21,713)               | -                   |
| Mortgage loans held-for-sale, net                     | -                      | -                         | 110,810                           | -                      | 110,810             |
| Other assets                                          | -                      | -                         | 15,791                            | 9                      | 15,800              |
| Total financial services assets                       | -                      | -                         | 245,637                           | (21,704)               | 223,933             |
| Total Assets                                          | \$2,726,034            | \$2,303,390               | \$ 245,637                        | \$(2,240,142)          | \$ 3,034,919        |
| <b>LIABILITIES AND EQUITY</b>                         |                        |                           |                                   |                        |                     |
| <b>Homebuilding:</b>                                  |                        |                           |                                   |                        |                     |
| Accounts payable                                      | \$39                   | \$58,531                  | \$ -                              | \$-                    | \$ 58,570           |
| Accrued liabilities                                   | 50,285                 | 132,666                   | -                                 | 2,180                  | 185,131             |
| Operating lease liabilities                           | 33,460                 | -                         | -                                 | -                      | 33,460              |
| Advances and notes payable to parent and subsidiaries | 28,222                 | 1,930,727                 | 296                               | (1,959,245)            | -                   |
| Revolving credit facility                             | 15,000                 | -                         | -                                 | -                      | 15,000              |
| Senior notes, net                                     | 988,322                | -                         | -                                 | -                      | 988,322             |
| Total homebuilding liabilities                        | 1,115,328              | 2,121,924                 | 296                               | (1,957,065)            | 1,280,483           |

**Financial Services:**

|                                                       |           |           |         |             |           |
|-------------------------------------------------------|-----------|-----------|---------|-------------|-----------|
| Accounts payable and other liabilities                | -         | -         | 61,054  | (2,180 )    | 58,874    |
| Advances and notes payable to parent and subsidiaries | -         | -         | 8,477   | (8,477 )    | -         |
| Mortgage repurchase facility                          | -         | -         | 84,856  | -           | 84,856    |
| Total financial services liabilities                  | -         | -         | 154,387 | (10,657 )   | 143,730   |
| Total Liabilities                                     | 1,115,328 | 2,121,924 | 154,683 | (1,967,722) | 1,424,213 |

**Equity:**

|                                            |             |             |           |               |             |
|--------------------------------------------|-------------|-------------|-----------|---------------|-------------|
| Total Stockholders' Equity                 | 1,610,706   | 181,466     | 90,954    | (272,420 )    | 1,610,706   |
| Total Liabilities and Stockholders' Equity | \$2,726,034 | \$2,303,390 | \$245,637 | \$(2,240,142) | \$3,034,919 |

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Table of Contents**Supplemental Condensed Combining Balance Sheet**

|                                                       | December 31, 2018      |                           |                                   |                        |                     |
|-------------------------------------------------------|------------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                                       | MDC                    | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|                                                       | (Dollars in thousands) |                           |                                   |                        |                     |
| <b>ASSETS</b>                                         |                        |                           |                                   |                        |                     |
| <b>Homebuilding:</b>                                  |                        |                           |                                   |                        |                     |
| Cash and cash equivalents                             | \$410,127              | \$4,597                   | \$ -                              | \$-                    | \$ 414,724          |
| Restricted cash                                       | -                      | 6,363                     | -                                 | -                      | 6,363               |
| Trade and other receivables                           | 758                    | 52,224                    | -                                 | -                      | 52,982              |
| Inventories:                                          |                        |                           |                                   |                        |                     |
| Housing completed or under construction               | -                      | 952,436                   | -                                 | -                      | 952,436             |
| Land and land under development                       | -                      | 1,180,558                 | -                                 | -                      | 1,180,558           |
| Total inventories                                     | -                      | 2,132,994                 | -                                 | -                      | 2,132,994           |
| Intercompany receivables                              | 1,735,342              | 7,369                     | -                                 | (1,742,711)            | -                   |
| Investment in subsidiaries                            | 455,848                | -                         | -                                 | (455,848 )             | -                   |
| Property and equipment, net                           | 23,896                 | 34,271                    | -                                 | -                      | 58,167              |
| Deferred tax assets, net                              | 36,168                 | -                         | -                                 | 1,010                  | 37,178              |
| Metropolitan district bond securities (related party) | -                      | -                         | -                                 | -                      | -                   |
| Other assets                                          | 12,234                 | 33,560                    | -                                 | -                      | 45,794              |
| Total Homebuilding Assets                             | 2,674,373              | 2,271,378                 | -                                 | (2,197,549)            | 2,748,202           |
| <b>Financial Services:</b>                            |                        |                           |                                   |                        |                     |
| Cash and cash equivalents                             | -                      | -                         | 49,052                            | -                      | 49,052              |
| Marketable securities                                 | -                      | -                         | 40,879                            | -                      | 40,879              |
| Intercompany receivables                              | -                      | -                         | 22,346                            | (22,346 )              | -                   |
| Mortgage loans held-for-sale, net                     | -                      | -                         | 149,211                           | -                      | 149,211             |
| Other assets                                          | -                      | -                         | 14,743                            | (1,010 )               | 13,733              |
| Total Financial Services Assets                       | -                      | -                         | 276,231                           | (23,356 )              | 252,875             |
| Total Assets                                          | \$2,674,373            | \$2,271,378               | \$ 276,231                        | \$(2,220,905)          | \$ 3,001,077        |
| <b>LIABILITIES AND EQUITY</b>                         |                        |                           |                                   |                        |                     |
| <b>Homebuilding:</b>                                  |                        |                           |                                   |                        |                     |
| Accounts payable                                      | \$-                    | \$50,505                  | \$ -                              | \$-                    | \$ 50,505           |
| Accrued liabilities                                   | 65,691                 | 125,387                   | -                                 | 5,169                  | 196,247             |
| Advances and notes payable to parent and subsidiaries | 29,715                 | 1,727,248                 | 295                               | (1,757,258)            | -                   |
| Revolving credit facility                             | 15,000                 | -                         | -                                 | -                      | 15,000              |
| Senior notes, net                                     | 987,967                | -                         | -                                 | -                      | 987,967             |
| Total Homebuilding Liabilities                        | 1,098,373              | 1,903,140                 | 295                               | (1,752,089)            | 1,249,719           |

**Financial Services:**

|                                                       |           |           |         |             |           |
|-------------------------------------------------------|-----------|-----------|---------|-------------|-----------|
| Accounts payable and accrued liabilities              | -         | -         | 63,712  | (5,169 )    | 58,543    |
| Advances and notes payable to parent and subsidiaries | -         | -         | 7,799   | (7,799 )    | -         |
| Mortgage repurchase facility                          | -         | -         | 116,815 | -           | 116,815   |
| Total Financial Services Liabilities                  | -         | -         | 188,326 | (12,968 )   | 175,358   |
| Total Liabilities                                     | 1,098,373 | 1,903,140 | 188,621 | (1,765,057) | 1,425,077 |

**Equity:**

|                                            |             |             |            |               |              |
|--------------------------------------------|-------------|-------------|------------|---------------|--------------|
| Total Stockholders' Equity                 | 1,576,000   | 368,238     | 87,610     | (455,848 )    | 1,576,000    |
| Total Liabilities and Stockholders' Equity | \$2,674,373 | \$2,271,378 | \$ 276,231 | \$(2,220,905) | \$ 3,001,077 |

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Table of Contents**Supplemental Condensed Combining Statement of Operations**

## Three Months Ended March 31, 2019

|                                                                                    | MDC                    | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|------------------------------------------------------------------------------------|------------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                                                                    | (Dollars in thousands) |                           |                                   |                        |                     |
| <b>Homebuilding:</b>                                                               |                        |                           |                                   |                        |                     |
| Revenues                                                                           | \$-                    | \$ 647,278                | \$ -                              | \$ -                   | \$ 647,278          |
| Cost of sales                                                                      | -                      | (524,552 )                | -                                 | -                      | (524,552 )          |
| Inventory impairments                                                              | -                      | (610 )                    | -                                 | -                      | (610 )              |
| Gross margin                                                                       | -                      | 122,116                   | -                                 | -                      | 122,116             |
| Selling, general, and administrative expenses                                      | (17,438)               | (64,701 )                 | -                                 | (122 )                 | (82,261 )           |
| Equity income of subsidiaries                                                      | 52,165                 | -                         | -                                 | (52,165 )              | -                   |
| Interest and other income                                                          | 2,409                  | 155                       | -                                 | (173 )                 | 2,391               |
| Other expense                                                                      | 7                      | (1,198 )                  | -                                 | -                      | (1,191 )            |
| Homebuilding pretax income (loss)                                                  | 37,143                 | 56,372                    | -                                 | (52,460 )              | 41,055              |
| <b>Financial Services:</b>                                                         |                        |                           |                                   |                        |                     |
| Financial services pretax income                                                   | -                      | -                         | 14,256                            | 295                    | 14,551              |
| Income before income taxes                                                         | 37,143                 | 56,372                    | 14,256                            | (52,165 )              | 55,606              |
| (Provision) benefit for income taxes                                               | 3,407                  | (15,264 )                 | (3,199 )                          | -                      | (15,056 )           |
| Net income                                                                         | \$40,550               | \$ 41,108                 | \$ 11,057                         | \$ (52,165 )           | \$ 40,550           |
| Other comprehensive income related to<br>available-for-sale securities, net of tax | -                      | -                         | -                                 | -                      | -                   |
| Comprehensive income                                                               | \$40,550               | \$ 41,108                 | \$ 11,057                         | \$ (52,165 )           | \$ 40,550           |

## Three Months Ended March 31, 2018

|                                               | MDC                    | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|-----------------------------------------------|------------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                               | (Dollars in thousands) |                           |                                   |                        |                     |
| <b>Homebuilding:</b>                          |                        |                           |                                   |                        |                     |
| Revenues                                      | \$-                    | \$ 607,688                | \$ -                              | \$ -                   | \$ 607,688          |
| Cost of sales                                 | -                      | (496,632 )                | -                                 | -                      | (496,632 )          |
| Inventory impairments                         | -                      | (550 )                    | -                                 | -                      | (550 )              |
| Gross margin                                  | -                      | 110,506                   | -                                 | -                      | 110,506             |
| Selling, general, and administrative expenses | (12,808)               | (58,329 )                 | -                                 | (204 )                 | (71,341 )           |
| Equity income of subsidiaries                 | 47,169                 | -                         | -                                 | (47,169 )              | -                   |
| Interest and other income                     | 1,773                  | 318                       | 2                                 | (234 )                 | 1,859               |
| Other expense                                 | 7                      | (570 )                    | -                                 | -                      | (563 )              |
| Homebuilding pretax income (loss)             | 36,141                 | 51,925                    | 2                                 | (47,607 )              | 40,461              |
| <b>Financial Services:</b>                    |                        |                           |                                   |                        |                     |
| Financial services pretax income              | -                      | -                         | 9,633                             | 438                    | 10,071              |
| Income before income taxes                    | 36,141                 | 51,925                    | 9,635                             | (47,169 )              | 50,532              |
| (Provision) benefit for income taxes          | 2,623                  | (12,092 )                 | (2,299 )                          | -                      | (11,768 )           |

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|                                                                                 |          |          |          |             |           |
|---------------------------------------------------------------------------------|----------|----------|----------|-------------|-----------|
| Net income                                                                      | \$38,764 | \$39,833 | \$ 7,336 | \$(47,169 ) | \$ 38,764 |
| Other comprehensive income related to available-for-sale securities, net of tax | -        | -        | -        | -           | -         |
| Comprehensive income                                                            | \$38,764 | \$39,833 | \$ 7,336 | \$(47,169 ) | \$ 38,764 |

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Table of Contents**Supplemental Condensed Combining Statement of Cash Flows**

|                                                      | Three Months Ended March 31, 2019 |                           |                                   |                        |                     |
|------------------------------------------------------|-----------------------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                                      | MDC                               | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|                                                      | (Dollars in thousands)            |                           |                                   |                        |                     |
| Net cash provided by (used in) operating activities  | \$(18,145 )                       | \$ 31,508                 | \$ 40,985                         | \$ -                   | \$ 54,348           |
| Net cash provided by (used in) investing activities  | 29,796                            | (6,094 )                  | (93 )                             | (30,043 )              | (6,434 )            |
| Financing activities:                                |                                   |                           |                                   |                        |                     |
| Payments from (advances to) subsidiaries             | -                                 | (23,614 )                 | (6,429 )                          | 30,043                 | -                   |
| Mortgage repurchase facility                         | -                                 | -                         | (31,959 )                         | -                      | (31,959 )           |
| Dividend payments                                    | (17,115 )                         | -                         | -                                 | -                      | (17,115 )           |
| Proceeds from exercise of stock options              | 7,087                             | -                         | -                                 | -                      | 7,087               |
| Net cash provided by (used in) financing activities  | (10,028 )                         | (23,614 )                 | (38,388 )                         | 30,043                 | (41,987 )           |
| Net increase (decrease) in cash and cash equivalents | 1,623                             | 1,800                     | 2,504                             | -                      | 5,927               |
| Cash and cash equivalents:                           |                                   |                           |                                   |                        |                     |
| Beginning of period                                  | 410,127                           | 10,960                    | 49,052                            | -                      | 470,139             |
| End of period                                        | \$411,750                         | \$ 12,760                 | \$ 51,556                         | \$ -                   | \$ 476,066          |

|                                                      | Three Months Ended March 31, 2018 |                           |                                   |                        |                     |
|------------------------------------------------------|-----------------------------------|---------------------------|-----------------------------------|------------------------|---------------------|
|                                                      | MDC                               | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminating<br>Entries | Consolidated<br>MDC |
|                                                      | (Dollars in thousands)            |                           |                                   |                        |                     |
| Net cash provided by (used in) operating activities  | \$(8,950 )                        | \$ (79,547 )              | \$ 27,011                         | \$ -                   | \$ (61,486 )        |
| Net cash provided by (used in) investing activities  | (94,576 )                         | (6,250 )                  | (60 )                             | 94,509                 | (6,377 )            |
| Financing activities:                                |                                   |                           |                                   |                        |                     |
| Payments from (advances to) subsidiaries             | -                                 | 83,203                    | 11,306                            | (94,509 )              | -                   |
| Mortgage repurchase facility                         | -                                 | -                         | (22,214 )                         | -                      | (22,214 )           |
| Dividend payments                                    | (16,865 )                         | -                         | -                                 | -                      | (16,865 )           |
| Proceeds from the exercise of stock options          | 282                               | -                         | -                                 | -                      | 282                 |
| Net cash provided by (used in) financing activities  | (16,583 )                         | 83,203                    | (10,908 )                         | (94,509 )              | (38,797 )           |
| Net increase (decrease) in cash and cash equivalents | (120,109)                         | (2,594 )                  | 16,043                            | -                      | (106,660 )          |
| Cash and cash equivalents:                           |                                   |                           |                                   |                        |                     |
| Beginning of period                                  | 468,718                           | 13,051                    | 32,471                            | -                      | 514,240             |



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|               |           |           |           |      |            |
|---------------|-----------|-----------|-----------|------|------------|
| End of period | \$348,609 | \$ 10,457 | \$ 48,514 | \$ - | \$ 407,580 |
|---------------|-----------|-----------|-----------|------|------------|

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Table of Contents**ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

The following discussion should be read in conjunction with, and is qualified in its entirety by, the Unaudited Consolidated Financial Statements and Notes thereto included elsewhere in this Quarterly Report on Form 10-Q. This item contains forward-looking statements that involve risks and uncertainties. The forward-looking statements are based upon management's experiences, observations, and analyses. Actual results may differ materially from those indicated in such forward-looking statements. Factors that may cause such a difference include, but are not limited to, those discussed in "Item 1A: Risk Factors" of our Annual Report on Form 10-K for the year ended December 31, 2018 and this Quarterly Report on Form 10-Q. The Company distributed an 8% stock dividend on February 28, 2019 to shareholders of record on February 14, 2019. In accordance with Accounting Standards Codification 260, "Earnings per Share," basic and diluted earnings per share amounts, weighted-average shares outstanding, and dividends declared per share have been restated for all periods presented to reflect the effect of this stock dividend.

|                                                 | Three Months Ended                                  |            |
|-------------------------------------------------|-----------------------------------------------------|------------|
|                                                 | March 31,                                           |            |
|                                                 | 2019                                                | 2018       |
|                                                 | (Dollars in thousands,<br>except per share amounts) |            |
| <b>Homebuilding:</b>                            |                                                     |            |
| Home sale revenues                              | \$647,278                                           | \$607,688  |
| Home cost of sales                              | (524,552 )                                          | (496,632 ) |
| Inventory impairments                           | (610 )                                              | (550 )     |
| Total cost of sales                             | (525,162 )                                          | (497,182 ) |
| Gross profit                                    | 122,116                                             | 110,506    |
| Gross margin                                    | 18.9 %                                              | 18.2 %     |
| Selling, general and administrative expenses    | (82,261 )                                           | (71,341 )  |
| Interest and other income                       | 2,391                                               | 1,859      |
| Other expense                                   | (1,191 )                                            | (563 )     |
| Homebuilding pretax income                      | 41,055                                              | 40,461     |
| <b>Financial Services:</b>                      |                                                     |            |
| Revenues                                        | 17,404                                              | 19,035     |
| Expenses                                        | (8,957 )                                            | (8,831 )   |
| Interest and other income                       | 1,264                                               | 1,020      |
| Net gain (loss) on marketable equity securities | 4,840                                               | (1,153 )   |
| Financial services pretax income                | 14,551                                              | 10,071     |
| Income before income taxes                      | 55,606                                              | 50,532     |
| Provision for income taxes                      | (15,056 )                                           | (11,768 )  |
| Net income                                      | \$40,550                                            | \$38,764   |
| Earnings per share:                             |                                                     |            |
| Basic                                           | \$0.66                                              | \$0.64     |

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|                                             |             |             |
|---------------------------------------------|-------------|-------------|
| Diluted                                     | \$0.64      | \$0.63      |
| Weighted average common shares outstanding: |             |             |
| Basic                                       | 60,939,364  | 60,340,774  |
| Diluted                                     | 62,708,334  | 61,447,563  |
| Dividends declared per share                | \$0.30      | \$0.28      |
| Cash provided by (used in):                 |             |             |
| Operating Activities                        | \$54,348    | \$(61,486 ) |
| Investing Activities                        | \$(6,434 )  | \$(6,377 )  |
| Financing Activities                        | \$(41,987 ) | \$(38,797 ) |

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*Overview*

*Three Months Ended March 31, 2019*

For the three months ended March 31, 2019, our net income was \$40.6 million, or \$0.64 per diluted share, a 5% increase compared to net income of \$38.8 million, or \$0.63 per diluted share, for the same period in the prior year. The increase was primarily the result of a \$4.5 million increase in our pretax income from financial services resulting from \$4.8 million of net gains on equity securities for the three months ended March 31, 2019 as compared to \$1.2 million of net losses on equity securities for the same period in the prior year. Our pretax income from homebuilding increased by only \$0.6 million year-over-year, as an \$11.6 million increase in homebuilding gross profit was mostly offset by higher selling, general and administrative costs. The increases in financial services and homebuilding pretax income were partially offset by a higher effective tax rate that was mostly due to federal energy tax credits, which reduced our 2018 first quarter income tax expense by \$1.2 million. It is currently uncertain as to the extent, if any, that energy tax credits will impact our 2019 results, and therefore no benefit was recorded for the 2019 first quarter.

Home sale revenues were up from \$607.7 million in the 2018 first quarter to \$647.3 million in the 2019 first quarter. The \$39.6 million year-over-year improvement was the result of a 7% increase in the number of homes delivered during the quarter.

The dollar value of our net new home orders decreased 1% from the prior year period driven by a 4% decrease in the average selling price, consistent with our ongoing focus on offering more affordable home plans. The decrease in the average selling price was also caused by a shift in the mix of home orders to our more affordable markets. However, the average selling price decrease was almost entirely offset by a 3% increase in the number of net new orders, resulting from a 15% increase in average active subdivisions that more than offset an 11% decrease in our monthly sales absorption pace.

*Industry Conditions and Outlook for MDC\**

We have experienced steadily improving net new order activity to start the year as monthly absorption rates remain healthy, albeit down from recent peak levels experienced in 2018. Overall, we believe industry conditions remain strong as we continued to see a positive economic environment driven by factors such as low unemployment, increasing wages, controlled inventory levels and low interest rates throughout the first quarter of 2019.

We have positioned ourselves for continued growth in the face of a slower monthly absorption pace environment, through achieving a 15% year-over-year increase in our active community count to end the first quarter of 2019. In addition, our backlog conversion rates have improved year-over-year, benefiting from lower cycle times for our more affordable home plans. The demand for affordable product lines remained strong during the first quarter of 2019, accounting for 60% of our net new orders compared to 44% in the prior year period.

Our dollar value of homes in backlog to end the 2019 first quarter was down 12% year-over-year to \$1.65 billion. This decrease is primarily the result of our continued focus on more affordable home plans, a shift in the mix of home sales to our more affordable markets and a lower pace of sales over the past six months.

Our liquidity to end the 2019 first quarter was up 27% year-over-year to \$1.49 billion, providing us with significant resources to fund continued growth. This increase was in large part due to the \$300 million increase in our homebuilding line of credit to \$1.0 billion during the fourth quarter of 2018.

\* See "**Forward-Looking Statements**" below.

Table of Contents*Homebuilding**Pretax Income:*

|                                  | Three Months<br>Ended  |          | Change  |       |
|----------------------------------|------------------------|----------|---------|-------|
|                                  | March 31,<br>2019      | 2018     | Amount  | %     |
|                                  | (Dollars in thousands) |          |         |       |
| West                             | \$33,200               | \$24,373 | \$8,827 | 36 %  |
| Mountain                         | 21,714                 | 24,185   | (2,471) | (10%) |
| East                             | 1,473                  | 3,375    | (1,902) | (56%) |
| Corporate                        | (15,332)               | (11,472) | (3,860) | (34%) |
| Total Homebuilding pretax income | \$41,055               | \$40,461 | \$594   | 1 %   |

For the three months ended March 31, 2019, we recorded homebuilding pretax income of \$41.1 million, an increase of \$0.6 million from \$40.5 million for the same period in the prior year. The increase was due to a 7% increase in home sale revenues and a 70 basis point improvement in our gross margin from home sales. However, these improvements were mostly offset by a 100 basis point increase in our selling, general and administrative expenses as a percentage of home sale revenues.

Our West segment experienced an \$8.8 million year-over-year improvement in pretax income, primarily due to a 16% increase in home sale revenues. Our Mountain segment experienced a \$2.5 million decrease in pretax income from the prior year period, primarily due to increased selling, general and administrative expenses driven by an increased average active community count. Our East segment experienced a \$1.9 million decrease in pretax income from the prior year, due to a 14% decrease in home sale revenues. Our Corporate Segment experienced a \$3.9 million year-over-year decrease in pretax income due to additional stock based compensation expense of \$3.0 million, primarily driven by performance-based stock awards.

*Assets:*

|          | March 31,              | December    | Change  |    |
|----------|------------------------|-------------|---------|----|
|          | 2019                   | 31,<br>2018 | Amount  | %  |
|          | (Dollars in thousands) |             |         |    |
| West     | \$1,307,761            | \$1,301,374 | \$6,387 | 0% |
| Mountain | 818,451                | 793,150     | 25,301  | 3% |

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|                           |             |             |          |    |
|---------------------------|-------------|-------------|----------|----|
| East                      | 170,670     | 169,485     | 1,185    | 1% |
| Corporate                 | 514,104     | 484,193     | 29,911   | 6% |
| Total homebuilding assets | \$2,810,986 | \$2,748,202 | \$62,784 | 2% |

Total homebuilding assets increased 2% from December 31, 2018 to March 31, 2019. The largest increase outside of our Corporate segment was in our Mountain segment and was the result of increases in our inventory balances. These increases were driven by land development spend and a greater number of homes completed or under construction as of period-end. The increase in our Corporate segment was the result of the adoption of ASC 842 on January 1, 2019, which requires a lessee to recognize a right-of-use asset and a corresponding lease liability for substantially all leases.

Table of Contents*New Home Deliveries & Home Sale Revenues:*

Changes in home sale revenues are impacted by changes in the number of new homes delivered and the average selling price of those delivered homes. Commentary for each of our segments on significant changes in these two metrics is provided below.

|                        | Three Months Ended March 31, |            |          | 2018  |            |          | % Change |           |         |     |    |
|------------------------|------------------------------|------------|----------|-------|------------|----------|----------|-----------|---------|-----|----|
|                        | 2019                         | Home Sale  | Average  | Homes | Home Sale  | Average  | Homes    | Home Sale | Average |     |    |
|                        | Homes                        | Revenues   | Price    |       | Revenues   | Price    |          | Revenues  | Price   |     |    |
| (Dollars in thousands) |                              |            |          |       |            |          |          |           |         |     |    |
| West                   | 752                          | \$ 369,558 | \$ 491.4 | 681   | \$ 319,509 | \$ 469.2 | 10%      | 16        | %       | 5   | %  |
| Mountain               | 409                          | 209,192    | 511.5    | 416   | 208,632    | 501.5    | (2 %)    | 0         | %       | 2   | %  |
| East                   | 197                          | 68,528     | 347.9    | 177   | 79,547     | 449.4    | 11%      | (14       | %)      | (23 | %) |
| Total                  | 1,358                        | \$ 647,278 | \$ 476.6 | 1,274 | \$ 607,688 | \$ 477.0 | 7 %      | 7         | %       | (0  | %) |

West Segment Commentary

Our West segment experienced a 10% year-over-year increase in the number of new homes delivered as a result of a 5% increase in the number of homes in backlog to start the quarter. Our California markets also benefited from an improved backlog conversion rate as there were a significant number of sales accepted at the end of 2017 that could not be delivered in the first quarter of 2018, which negatively impacted our prior year backlog conversion rate. The 5% increase in average selling price of homes delivered is the result of price increases we implemented across most markets during the 2018 spring selling season, which were partially offset by a shift in mix in our California markets to lower priced communities.

Mountain Segment Commentary

While the number of homes in backlog to start the quarter was down 17% year-over-year, new homes delivered decreased by only 2% due to an improved backlog conversion rate that was driven by (1) shorter average cycle times and (2) a higher percentage of homes both sold and delivered in the first quarter of 2019 as compared to the 2018 first quarter. Cycle time improvements were primarily driven by our Colorado markets as a result of a vendor related product defect issue that negatively impacted cycle times for those homes delivered in the first half of 2018. The average selling price of homes delivered increased 2% as a result of price increases implemented in the first half of 2018 in our Colorado markets.

East Segment Commentary



The 23% decrease in the average selling price of homes delivered in our East segment is due to a change in mix resulting from (1) a higher percentage of our deliveries coming from our Florida markets, which have a lower average selling price than our mid-Atlantic market and (2) a higher percentage of deliveries in this segment coming from communities that offer more affordable home plans. The 11% increase in new home deliveries was driven by an increased backlog conversion rate across all markets as a result of (1) a decrease in cancellation rates and (2) a higher percentage of deliveries from our more affordable product offerings, which typically have shorter cycle times than our more traditional products.

Table of Contents*Gross Margin from Home Sales:*

Our gross margin from home sales for the three months ended March 31, 2019 increased 70 basis points year-over-year from 18.2% to 18.9%. During the three months ended March 31, 2019 and 2018, we recorded \$0.9 million and \$3.1 million of expense to adjust our warranty accrual. The adjustments to our warranty accrual negatively impacted gross margin by 10 basis points and 50 basis points, respectively. Our gross margin from home sales in the 2019 first quarter was positively impacted by a 20 basis point improvement in our capitalized interest in cost of sales as a percentage of home sale revenues, while the 2018 first quarter benefited by 20 basis points due to recoveries from a vendor as a result of product defect related issues.

*Inventory Impairments:*

Impairments of homebuilding inventory by segment for the three months ended March 31, 2019 and 2018 are shown in the table below:

|                             | Three<br>Months<br>Ended<br>March 31,<br>2019 2018<br>(Dollars in<br>thousands) |       |
|-----------------------------|---------------------------------------------------------------------------------|-------|
| West                        | \$-                                                                             | \$375 |
| Mountain                    | 400                                                                             | 175   |
| East                        | 210                                                                             | -     |
| Total inventory impairments | \$610                                                                           | \$550 |

The table below provides quantitative data, for the periods presented, used in determining the fair value of the impaired inventory.

| Three Months Ended | Impairment Data                           |                                        | Number of<br>Subdivisions<br>Impaired | Quantitative             |
|--------------------|-------------------------------------------|----------------------------------------|---------------------------------------|--------------------------|
|                    | Total Inventory<br>Subdivisions<br>Tested | Fair Value<br>of<br>Inventory<br>After |                                       | Data<br>Discount<br>Rate |

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|                | Impairments            |    |     |    |        |   |      |
|----------------|------------------------|----|-----|----|--------|---|------|
|                | (Dollars in thousands) |    |     |    |        |   |      |
| March 31, 2019 | 16                     | \$ | 610 | \$ | 10,476 | 2 | N/A  |
| March 31, 2018 | 24                     | \$ | 550 | \$ | 5,223  | 2 | 12 % |

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Table of Contents*Selling, General and Administrative Expenses:*

|                                                                                          | Three Months Ended March 31, |          |          |
|------------------------------------------------------------------------------------------|------------------------------|----------|----------|
|                                                                                          | 2019                         | 2018     | Change   |
|                                                                                          | (Dollars in thousands)       |          |          |
| General and administrative expenses                                                      | \$42,572                     | \$35,753 | \$6,819  |
| General and administrative expenses as a percentage of home sale revenues                | 6.6 %                        | 5.9 %    | 70 bps   |
| Marketing expenses                                                                       | \$18,296                     | \$15,571 | \$2,725  |
| Marketing expenses as a percentage of home sale revenues                                 | 2.8 %                        | 2.6 %    | 20 bps   |
| Commissions expenses                                                                     | \$21,393                     | \$20,017 | \$1,376  |
| Commissions expenses as a percentage of home sale revenues                               | 3.3 %                        | 3.3 %    | 0 bps    |
| Total selling, general and administrative expenses                                       | \$82,261                     | \$71,341 | \$10,920 |
| Total selling, general and administrative expenses as a percentage of home sale revenues | 12.7 %                       | 11.7 %   | 100 bps  |

For the three months ended March 31, 2019, the increases in our general and administrative expenses were due to increased compensation-related expenses driven by higher average headcount and additional stock based compensation expense of \$3.0 million, primarily caused by the performance-based stock awards that were granted in 2017.

Our marketing expenses increased for the three months ended March 31, 2019 due to increased sales office and model home expenses resulting from a 15% increase in active subdivisions as well as increased compensation-related expenses driven by higher average headcount.

Table of Contents**Other Homebuilding Operating Data***Net New Orders and Active Subdivisions:*

|          | Three Months Ended March 31,<br>2019 |              |               |                           | 2018  |              |               |                           | % Change |              |               |                         |
|----------|--------------------------------------|--------------|---------------|---------------------------|-------|--------------|---------------|---------------------------|----------|--------------|---------------|-------------------------|
|          | Homes                                | Dollar Value | Average Price | Monthly Absorption Rate * | Homes | Dollar Value | Average Price | Monthly Absorption Rate * | Homes    | Dollar Value | Average Price | Monthly Absorption Rate |
|          | (Dollars in thousands)               |              |               |                           |       |              |               |                           |          |              |               |                         |
| West     | 965                                  | \$433,307    | \$449.0       | 3.82                      | 1,033 | \$458,195    | \$443.6       | 4.78                      | (7 %)    | (5 %)        | 1 %           | (20 %)                  |
| Mountain | 719                                  | 336,932      | 468.6         | 3.52                      | 667   | 327,006      | 490.3         | 3.92                      | 8 %      | 3 %          | (4 %)         | (10 %)                  |
| East     | 272                                  | 81,179       | 298.5         | 4.17                      | 204   | 78,459       | 384.6         | 2.99                      | 33%      | 3 %          | (22 %)        | 39 %                    |
| Total    | 1,956                                | \$851,418    | \$435.3       | 3.75                      | 1,904 | \$863,660    | \$453.6       | 4.19                      | 3 %      | (1 %)        | (4 %)         | (11 %)                  |

\*Calculated as total net new orders in period ÷ average active communities during period ÷ number of months in period

|          | Active Subdivisions |      |          | Average Active Subdivisions  |      |        |   |
|----------|---------------------|------|----------|------------------------------|------|--------|---|
|          | March 31, 2019      | 2018 | Change % | Three Months Ended March 31, |      |        | % |
|          | 2019                | 2018 | Change   | 2019                         | 2018 | Change | % |
| West     | 88                  | 73   | 21 %     | 84                           | 72   | 17 %   | % |
| Mountain | 64                  | 58   | 10 %     | 69                           | 57   | 21 %   | % |
| East     | 26                  | 24   | 8 %      | 22                           | 23   | (4 %)  | % |
| Total    | 178                 | 155  | 15 %     | 175                          | 152  | 15 %   | % |

West Segment Commentary

For the three months ended March 31, 2019, the dollar value of net new orders decreased 5% year-over-year, driven by a 7% decrease in the number of net new orders. The lower number of net new orders was the result of a 20% decrease in the monthly sales absorption rate. While all markets experienced a decline in their sales pace year-over-year, California was the main driver of the decline as a result of: (1) a smaller relative proportion of affordable product offerings currently available in this market and (2) an increased cancellation rate (see further discussion below). The decline in our sales pace was mostly offset by a 17% increase in average active community count as all markets experienced a double digit percentage increase in average active community count with the exception of Arizona, which was flat year-over-year. Oregon, our newest market, finished the quarter with two active communities compared with none a year ago.

Mountain Segment Commentary

For the three months ended March 31, 2019, the dollar value of net new orders increased 3% from the same period in the prior year primarily due to an 8% increase in our number of net new orders. Our higher number of net new orders was the result of a 21% increase in average active community count as a result of growth in Utah where we continue to see strong potential and have increased our community count accordingly. This increase was partially offset by a 10% decrease in monthly sales absorption pace. Colorado and Utah both experienced a decline in sales pace consistent with industry trends, with Utah further impacted by an increased cancellation rate (see further discussion below).

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Table of ContentsEast Segment Commentary

For the three months ended March 31, 2019, our dollar values of net new orders increased 3% from the same period in 2018 as a 39% improvement in our monthly sales absorption rate was largely offset by a 22% decline in our average selling price of net new orders. The improved sales pace was primarily due to an increased offering of more affordable products in our Florida markets, which have realized a higher selling pace. The sales pace in our Florida markets also benefited from a decreased cancellation rate (see further discussion below). Our average active community count was down slightly due to decreased land acquisition activity in the mid-Atlantic region over the past two years where we have invested less because our returns in this market had been lower than expected. However, as noted above, we have recently experienced improving returns in the mid-Atlantic region resulting in our reinvestment in this market. The decrease in the average selling price of net new orders is due to mix as a result of: (1) a higher percentage of our net new orders coming from an expanded offering of more affordable home plans, due to an increasing level of demand for these plans, and (2) a higher percentage of our net new orders coming from our Florida markets, which have a lower average selling price than our mid-Atlantic operations.

*Cancellation Rate:*

|          | Cancellations as a<br>Percentage of |      | Homes in Beginning<br>Backlog<br>Three<br>Months |    | Change in  |
|----------|-------------------------------------|------|--------------------------------------------------|----|------------|
|          | Ended                               |      | March 31,                                        |    | Percentage |
|          | 2019                                | 2018 | %                                                | %  |            |
| West     | 14%                                 | 14%  | 0                                                | 0  | %          |
| Mountain | 14%                                 | 11%  | 3                                                | 11 | %          |
| East     | 11%                                 | 23%  | (12)                                             | 12 | (%)        |
| Total    | 14%                                 | 14%  | 0                                                | 0  | %          |

Our cancellations as a percentage of homes in beginning backlog to start the quarter (“cancellation rate”) remained unchanged year-over-year. Our East segment experienced the largest percentage decrease as we saw double digit percentage improvements across all markets. In addition, the cancellation rate in our Florida (East segment) markets benefited from the implementation of additional underwriting procedures prior to the acceptance of new home contracts. Our Utah (Mountain segment) and Southern California (West segment) markets experienced the largest percentage increases year-over-year. The increase in Utah was primarily due to a shift in mix to include more first-time homebuyers, who have a higher likelihood of cancellation, while the increase in Southern California is largely due to homebuyer uncertainty as a result of affordability concerns.





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|          | March 31,<br>2019      |                 |                  | 2018  |                 |                  | % Change |                 |                  |
|----------|------------------------|-----------------|------------------|-------|-----------------|------------------|----------|-----------------|------------------|
|          | Homes                  | Dollar<br>Value | Average<br>Price | Homes | Dollar<br>Value | Average<br>Price | Homes    | Dollar<br>Value | Average<br>Price |
|          | (Dollars in thousands) |                 |                  |       |                 |                  |          |                 |                  |
| West     | 1,736                  | \$830,703       | \$478.5          | 1,803 | \$923,326       | \$512.1          | (4 %)    | (10 %)          | (7 %)            |
| Mountain | 1,353                  | 690,623         | 510.4            | 1,504 | 766,010         | 509.3            | (10%)    | (10 %)          | 0 %              |
| East     | 445                    | 133,140         | 299.2            | 482   | 190,102         | 394.4            | (8 %)    | (30 %)          | (24 %)           |
| Total    | 3,534                  | \$1,654,466     | \$468.2          | 3,789 | \$1,879,438     | \$496.0          | (7 %)    | (12 %)          | (6 %)            |

At March 31, 2019, we had 3,534 homes in backlog with a total value of \$1.65 billion, representing respective decreases of 7% and 12% from March 31, 2018. The majority of our markets experienced a year-over-year decline in both the number of homes in backlog and the average selling price of those homes to end the quarter. The decrease in the number of homes in backlog is primarily a result of the year-over-year decrease in net new orders in the fourth quarter of 2018 coupled with an increase in backlog conversion rates due to improved cycle times. The decrease in the average selling price of homes in backlog is due to a shift in mix to lower priced communities, consistent with our focus on offering more affordable home plans, as well as a shift in geographical mix with an increased proportion of net new orders coming from our Arizona (West segment) and Florida (East segment) markets, which have the lowest average selling prices in our Company.

*Homes Completed or Under Construction (WIP lots):*

|                                             | March 31, |       | % Change |   |
|---------------------------------------------|-----------|-------|----------|---|
|                                             | 2019      | 2018  |          |   |
| Unsold:                                     |           |       |          |   |
| Completed                                   | 120       | 86    | 40       | % |
| Under construction                          | 177       | 203   | (13)     | % |
| Total unsold started homes                  | 297       | 289   | 3        | % |
| Sold homes under construction or completed  | 2,362     | 2,549 | (7)      | % |
| Model homes under construction or completed | 459       | 366   | 25       | % |
| Total homes completed or under construction | 3,118     | 3,204 | (3)      | % |

Our model homes under construction or completed were up 25% despite our active community count being up only 15% year-over-year. This is primarily the result of models being constructed to open new communities in the near future as we plan for growth in our active community count.



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*Lots Owned and Optioned (including homes completed or under construction):*

|          | March 31, 2019 |               |        | March 31, 2018 |               |        | Total |        |
|----------|----------------|---------------|--------|----------------|---------------|--------|-------|--------|
|          | Lots Owned     | Lots Optioned | Total  | Lots Owned     | Lots Optioned | Total  | %     | Change |
| West     | 7,894          | 2,462         | 10,356 | 7,421          | 2,205         | 9,626  | 8     | %      |
| Mountain | 6,636          | 2,612         | 9,248  | 5,206          | 3,398         | 8,604  | 7     | %      |
| East     | 1,989          | 1,294         | 3,283  | 1,531          | 1,692         | 3,223  | 2     | %      |
| Total    | 16,519         | 6,368         | 22,887 | 14,158         | 7,295         | 21,453 | 7     | %      |

Our total owned and optioned lots at March 31, 2019 were 22,887, up 7% from March 31, 2018, due to our increased land acquisition approval activity over the past year across all markets. We believe that our total lot supply, coupled with our planned acquisition activity, can support growth in future periods. See "**Forward-Looking Statements**" below.

**Financial Services**

|                                        | Three Months Ended |                |               |          |
|----------------------------------------|--------------------|----------------|---------------|----------|
|                                        | March 31, 2019     | March 31, 2018 | Change Amount | Change % |
| (Dollars in thousands)                 |                    |                |               |          |
| Financial services revenues            |                    |                |               |          |
| Mortgage operations                    | \$10,174           | \$12,696       | \$(2,522)     | (20 %)   |
| Other                                  | 7,230              | 6,339          | 891           | 14 %     |
| Total financial services revenues      | \$17,404           | \$19,035       | \$(1,631)     | (9 %)    |
| Financial services pretax income       |                    |                |               |          |
| Mortgage operations                    | \$4,993            | \$7,520        | \$(2,527)     | (34 %)   |
| Other                                  | 9,558              | 2,551          | 7,007         | 275 %    |
| Total financial services pretax income | \$14,551           | \$10,071       | \$4,480       | 44 %     |

For the three months ended March 31, 2019, our financial services pretax income increased \$4.5 million, or 44%, from the same period in the prior year. The increase was primarily due to our other financial services segment and was driven by \$4.8 million of net gains on equity securities for the three months ended March 31, 2019 as compared to \$1.2 million of net losses on equity securities for the three months ended March 31, 2018. This was partially offset by a decrease in our mortgage operations segment, which saw a decrease in the capture rate of new home deliveries and an increase in special financing offers year-over-year, both of which negatively impacted pretax income for the three

months ended March 31, 2019.

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The following table sets forth information for our mortgage operations segment relating to mortgage loans originated and capture rate.

|                                                                | Three Months Ended<br>March 31, |           | % or<br>Percentage<br>Change |    |
|----------------------------------------------------------------|---------------------------------|-----------|------------------------------|----|
|                                                                | 2019                            | 2018      |                              |    |
|                                                                | (Dollars in thousands)          |           |                              |    |
| Total Originations (including transfer loans):                 |                                 |           |                              |    |
| Loans                                                          | 783                             | 807       | (3                           | %) |
| Principal                                                      | \$285,525                       | \$298,070 | (4                           | %) |
| Capture Rate Data:                                             |                                 |           |                              |    |
| Capture rate as % of all homes delivered                       | 58                              | % 63      | % (5                         | %) |
| Capture rate as % of all homes delivered (excludes cash sales) | 62                              | % 68      | % (6                         | %) |
| Mortgage Loan Origination Product Mix:                         |                                 |           |                              |    |
| FHA loans                                                      | 17                              | % 14      | % 3                          | %) |
| Other government loans (VA & USDA)                             | 20                              | % 19      | % 1                          | %) |
| Total government loans                                         | 37                              | % 33      | % 4                          | %) |
| Conventional loans                                             | 63                              | % 67      | % (4                         | %) |
|                                                                | 100                             | % 100     | % 0                          | %) |
| Loan Type:                                                     |                                 |           |                              |    |
| Fixed rate                                                     | 96                              | % 97      | % (1                         | %) |
| ARM                                                            | 4                               | % 3       | % 1                          | %) |
| Credit Quality:                                                |                                 |           |                              |    |
| Average FICO Score                                             | 736                             | 744       | (1                           | %) |
| Other Data:                                                    |                                 |           |                              |    |
| Average Combined LTV ratio                                     | 81                              | % 81      | % 0                          | %) |
| Full documentation loans                                       | 100                             | % 100     | % 0                          | %) |
| Loans Sold to Third Parties:                                   |                                 |           |                              |    |
| Loans                                                          | 889                             | 873       | 2                            | %) |
| Principal                                                      | \$320,414                       | \$320,753 | (0                           | %) |

***Income Taxes***

Our overall effective income tax rates were 27.1% and 23.3% for the three months ended March 31, 2019 and 2018, respectively, resulting in income tax expense of \$15.1 million and \$11.8 million for the same periods, respectively. The year-over-year increase in our effective tax rate for the three months ended March 31, 2019 was due to a \$1.2 million benefit from energy tax credits which reduced our 2018 first quarter tax rate. It is currently uncertain as to the extent, if any, that energy tax credits will impact our 2019 results, and therefore no benefit was recorded for the 2019 first quarter.



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**CRITICAL ACCOUNTING ESTIMATES AND POLICIES**

The preparation of financial statements in conformity with accounting policies generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Management evaluates such estimates and judgments on an on-going basis and makes adjustments as deemed necessary. Actual results could differ from these estimates if conditions are significantly different in the future. See "**Forward-Looking Statements**" below.

Our critical accounting estimates and policies have not changed from those reported in Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2018.

**LIQUIDITY AND CAPITAL RESOURCES**

We use our liquidity and capital resources to: (1) support our operations, including the purchase of land, land development and construction of homes; (2) provide working capital; and (3) provide mortgage loans for our homebuyers. Our liquidity includes our cash and cash equivalents, marketable securities, Revolving Credit Facility and Mortgage Repurchase Facility (both defined below). Additionally, we have an existing effective shelf registration statement that allows us to issue equity, debt or hybrid securities up to \$1.35 billion.

We have marketable equity securities that consist primarily of holdings in common stock and exchange traded funds.

**Capital Resources**

Our capital structure is primarily a combination of (1) permanent financing, represented by stockholders' equity; (2) long-term financing, represented by our 5 % senior notes due 2020, 5½% senior notes due 2024 and our 6% senior notes due 2043; (3) our Revolving Credit Facility (defined below) and (4) our Mortgage Repurchase Facility (defined below). Because of our current balance of cash, cash equivalents, marketable securities, ability to access the capital markets, and available capacity under both our Revolving Credit Facility and Mortgage Repurchase Facility, we believe that our capital resources are adequate to satisfy our short and long-term capital requirements, including

meeting future payments on our senior notes as they become due. See "**Forward-Looking Statements**" below.

We may from time to time seek to retire or purchase our outstanding senior notes through cash purchases, whether through open market purchases, privately negotiated transactions or otherwise. Such repurchases, if any, will depend on prevailing market conditions, our liquidity requirements, contractual restrictions and other factors. The amounts involved may be material.

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**Senior Notes, Revolving Credit Facility and Mortgage Repurchase Facility**

*Senior Notes.* Our senior notes are not secured and, while the senior note indentures contain some restrictions on secured debt and other transactions, they do not contain financial covenants. Our senior notes are fully and unconditionally guaranteed on an unsecured basis, jointly and severally, by most of our homebuilding segment subsidiaries. We believe that we are in compliance with the representations, warranties and covenants in the senior note indentures.

*Revolving Credit Facility.* We have an unsecured revolving credit agreement (“Revolving Credit Facility”) with a group of lenders which may be used for general corporate purposes. This agreement was amended on November 1, 2018 to (1) extend the Revolving Credit Facility maturity to December 18, 2023, (2) increase the aggregate commitment from \$700 million to \$1.0 billion (the “Commitment”) and (3) provide that the aggregate amount of the commitments may increase to an amount not to exceed \$1.5 billion upon our request, subject to receipt of additional commitments from existing or additional lenders and, in the case of additional lenders, the consent of the co-administrative agents. As defined in the Revolving Credit Facility, interest rates on base rate borrowings are equal to the highest of (1) 0.0%, (2) a prime rate, (3) a federal funds effective rate plus 1.50%, and (4) a specified eurocurrency rate plus 1.00% and, in each case, plus a margin that is determined based on our credit ratings and leverage ratio. Interest rates on eurocurrency borrowings are equal to a specified eurocurrency rate plus a margin that is determined based on our credit ratings and leverage ratio. At any time at which our leverage ratio, as of the last day of the most recent calendar quarter, exceeds 55%, the aggregate principal amount of all consolidated senior debt borrowings outstanding may not exceed the borrowing base. There is no borrowing base requirement if our leverage ratio, as of the last day of the most recent calendar quarter, is 55% or less.

The Revolving Credit Facility is fully and unconditionally guaranteed, jointly and severally, by most of our homebuilding segment subsidiaries. The facility contains various representations, warranties and covenants that we believe are customary for agreements of this type. The financial covenants include a consolidated tangible net worth test and a leverage test, along with a consolidated tangible net worth covenant, all as defined in the Revolving Credit Facility. A failure to satisfy the foregoing tests does not constitute an event of default, but can trigger a “term-out” of the facility. A breach of the consolidated tangible net worth covenant (but not the consolidated tangible net worth test) or a violation of anti-corruption or sanctions laws would result in an event of default.

The Revolving Credit Facility is subject to acceleration upon certain specified events of default, including breach of the consolidated tangible net worth covenant, a violation of anti-corruption or sanctions laws, failure to make timely payments, breaches of certain representations or covenants, failure to pay other material indebtedness, or another person becoming beneficial owner of 50% or more of our outstanding common stock. We believe we were in compliance with the representations, warranties and covenants included in the Revolving Credit Facility as of March 31, 2019.

We incur costs associated with unused commitment fees pursuant to the terms of the Revolving Credit Facility. At March 31, 2019 and December 31, 2018, there were \$27.6 million and \$27.8 million, respectively, in letters of credit outstanding, which reduced the amounts available to be borrowed under the Revolving Credit Facility. We had \$15.0 million outstanding under the Revolving Credit Facility as of March 31, 2019 and December 31, 2018. As of March 31, 2019, availability under the Revolving Credit Facility was approximately \$957.4 million.

*Mortgage Repurchase Facility.* HomeAmerican has a Master Repurchase Agreement (the “Mortgage Repurchase Facility”) with U.S. Bank National Association (“USBNA”). Effective August 9, 2018, the Mortgage Repurchase Facility was amended to extend its termination date to August 8, 2019. The Mortgage Repurchase Facility provides liquidity to HomeAmerican by providing for the sale of up to an aggregate of \$75 million (subject to increase by up to \$75 million under certain conditions) of eligible mortgage loans to USBNA with an agreement by HomeAmerican to repurchase the mortgage loans at a future date. Until such mortgage loans are transferred back to HomeAmerican, the documents relating to such loans are held by USBNA, as custodian, pursuant to the Custody Agreement (“Custody Agreement”), dated as of November 12, 2008, by and between HomeAmerican and USBNA. In the event that an eligible mortgage loan becomes ineligible, as defined under the Mortgage Repurchase Facility, HomeAmerican may be required to repurchase the ineligible mortgage loan immediately. The maximum aggregate commitment of the Mortgage Repurchase Facility was temporarily increased on March 27, 2019 from \$75 million to \$100 million and was effective through April 24, 2019. The Mortgage Repurchase Facility also had a temporary increase in the maximum aggregate commitment from \$75 million to \$130 million on December 27, 2018 and was effective through January 25, 2019. At March 31, 2019 and December 31, 2018, HomeAmerican had \$84.9 million and \$116.8 million, respectively, of mortgage loans that HomeAmerican was obligated to repurchase under the Mortgage Repurchase Facility. Mortgage loans that HomeAmerican is obligated to repurchase under the Mortgage Repurchase Facility are accounted for as a debt financing arrangement and are reported as mortgage repurchase facility in the consolidated balance sheets. Advances under the Mortgage Repurchase Facility carry a price range that is based on a LIBOR rate or successor benchmark rate.

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The Mortgage Repurchase Facility contains various representations, warranties and affirmative and negative covenants that we believe are customary for agreements of this type. The negative covenants include, among others, (i) a minimum Adjusted Tangible Net Worth requirement, (ii) a maximum Adjusted Tangible Net Worth ratio, (iii) a minimum adjusted net income requirement, and (iv) a minimum Liquidity requirement. The foregoing capitalized terms are defined in the Mortgage Repurchase Facility. We believe HomeAmerican was in compliance with the representations, warranties and covenants included in the Mortgage Repurchase Facility as of March 31, 2019.

## **Dividends**

During the three months ended March 31, 2019 and 2018, we paid dividends of \$0.30 per share and \$0.28 per share, respectively.

## **MDC Common Stock Repurchase Program**

At March 31, 2019, we were authorized to repurchase up to 4,000,000 shares of our common stock. We did not repurchase any shares of our common stock during the three months ended March 31, 2019.

## **Consolidated Cash Flow**

During the three months ended March 31, 2019, we generated \$54.3 million of cash from operating activities, primarily due to: 1) net income of \$40.6 million, 2) a net decrease in mortgage loans held-for-sale of \$38.4 million, 3) non-cash add-backs to net income related to depreciation and stock-based compensation totaling \$9.1 million and 4) a decrease in our net deferred tax assets of \$2.7 million. These amounts were partially offset by: 1) a net increase in land and land under development of \$18.5 million, 2) a net increase in trade and other receivables of \$13.8 million and 3) net gains on marketable equity securities of \$4.8 million.

During the three months ended March 31, 2019, we used \$6.4 million of cash for investing activities, due to the purchase of \$6.4 million in property and equipment.

During the three months ended March 31, 2019, we used \$42.0 million of cash for financing activities, primarily related to net payments on our mortgage repurchase facility of \$32.0 million and dividend payments totaling \$17.1 million. These amounts were slightly offset by proceeds of \$7.1 million from the exercise of stock options.

## Off-Balance Sheet Arrangements

*Lot Option Purchase Contracts.* In the ordinary course of business, we enter into lot option purchase contracts in order to procure lots for the construction of homes. Lot option contracts enable us to control lot positions with a minimal capital investment, which substantially reduces the risks associated with land ownership and development. At March 31, 2019, we had deposits of \$22.0 million in the form of cash and \$5.4 million in the form of letters of credit that secured option contracts to purchase 6,368 lots for a total estimated purchase price of \$463.1 million.

*Surety Bonds and Letters of Credit.* At March 31, 2019, we had outstanding surety bonds and letters of credit totaling \$245.5 million and \$89.3 million, respectively, including \$61.7 million in letters of credit issued by HomeAmerican. The estimated cost to complete obligations related to these bonds and letters of credit was approximately \$126.6 million and \$51.2 million, respectively. We expect that the obligations secured by these performance bonds and letters of credit generally will be performed in the ordinary course of business and in accordance with the applicable contractual terms. To the extent that the obligations are performed, the related performance bonds and letters of credit should be released and we should not have any continuing obligations. However, in the event any such performance bonds or letters of credit are called, our indemnity obligations could require us to reimburse the issuer of the performance bond or letter of credit.

We have made no material guarantees with respect to third-party obligations.

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**IMPACT OF INFLATION, CHANGING PRICES AND ECONOMIC CONDITIONS**

The impact of inflation and changing prices have not changed materially from the disclosure in our December 31, 2018 Annual Report on Form 10-K.

**OTHER**

**Forward-Looking Statements**

Certain statements in this Quarterly Report on Form 10-Q, as well as statements made by us in periodic press releases, oral statements made by our officials in the course of presentations about the Company and conference calls in connection with quarterly earnings releases, constitute “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include statements regarding our business, financial condition, results of operations, cash flows, strategies and prospects. These forward-looking statements may be identified by terminology such as “likely,” “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “potential” or “continue,” or the negative of such terms and other comparable terminology. Although we believe that the expectations reflected in the forward-looking statements contained in this Report are reasonable, we cannot guarantee future results. These statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company to be materially different from those expressed or implied by the forward-looking statements. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise. However, any further disclosures made on related subjects in subsequent reports on Forms 10-K, 10-Q and 8-K should be considered. Additionally, information about issues that could lead to material changes in performance and risk factors that have the potential to affect us is contained under the caption “Risk Factors” in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2018 and Item 1A of Part II of this Quarterly Report on Form 10-Q.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

We have a cash and investment policy that enables us to achieve an appropriate investment return while preserving principal and managing risk. Under this policy, our cash and cash equivalents may include U.S. government securities, commercial bank deposits, commercial paper, certificates of deposit, money market funds, and time deposits, with maturities of three months or less. Our marketable securities under this policy may include holdings in U.S. government securities with a maturity of more than three months, equity securities and corporate debt securities.

The market value and/or income derived from our equity securities may go up or down, sometimes rapidly or unpredictably. Equity securities may decline in value due to factors affecting equity securities markets generally, particular industries represented in those markets, or the issuer itself. The values of equity securities may decline due

to general market conditions that are not specifically related to a particular company, such as real or perceived adverse economic conditions, changes in the general outlook for corporate earnings, changes in interest or currency rates or adverse investor sentiment generally. They may also decline due to factors that affect a particular industry or industries, such as labor shortages or increased production costs and competitive conditions within an industry. The value of equity securities may also decline for a number of other reasons that directly relate to the issuer, such as management performance, financial leverage, the issuer's historical and prospective earnings, the value of its assets and reduced demand for its goods and services. Equity securities generally have greater price volatility than bonds and other debt securities.

As of March 31, 2019, our cash and cash equivalents included U.S. government securities, commercial bank deposits, money market funds and time deposits, with maturities of three months or less. As of March 31, 2019, our marketable securities included holdings in common stock and exchange traded funds.

We are exposed to market risks related to fluctuations in interest rates on mortgage loans held-for-sale, mortgage interest rate lock commitments and debt. Derivative instruments utilized in the normal course of business by HomeAmerican include interest rate lock commitments and forward sales of mortgage-backed securities, which are used to manage the price risk on fluctuations in interest rates on our mortgage loans in inventory and interest rate lock commitments to originate mortgage loans. Such contracts are the only significant financial derivative instruments utilized by MDC. HomeAmerican's mortgage loans in process for which a rate and price commitment had been made to a borrower that had not closed at March 31, 2019 had an aggregate principal balance of \$149.4 million, all of which were under interest rate lock commitments at an average interest rate of 4.30%. In addition, HomeAmerican had mortgage loans held-for-sale with an aggregate principal balance of \$107.0 million at March 31, 2019, of which \$14.1 million had not yet been committed to a mortgage purchaser and had an average interest rate of 4.47%. In order to hedge the changes in fair value of interest rate lock commitments and mortgage loans held-for-sale which had not yet been committed to a mortgage purchaser, HomeAmerican had forward sales of securities totaling \$121.0 million and \$65.5 million at March 31, 2019 and December 31, 2018, respectively.

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HomeAmerican provides mortgage loans that generally are sold forward and subsequently delivered to a third-party purchaser between 10 and 35 days. Forward commitments are used for non-trading purposes to sell mortgage loans and hedge price risk due to fluctuations in interest rates on rate-locked mortgage loans in process that have not closed. Due to this economic hedging philosophy, the market risk associated with these mortgages is limited. For forward sales commitments, as well as commitments to originate mortgage loans that are still outstanding at the end of a reporting period, we record the fair value of the derivatives in the consolidated statements of operations and comprehensive income with an offset to either derivative assets or liabilities, depending on the nature of the change.

We utilize our Revolving Credit Facility, our Mortgage Repurchase Facility and senior notes in our financing strategy. For fixed rate debt, changes in interest rates generally affect the fair value of the debt instrument, but do not affect our earnings or cash flows. We do not have an obligation to prepay our senior notes prior to maturity and, as a result, interest rate risk and changes in fair value do not have an impact on our financial position, results of operations or cash flows. For variable rate debt such as our Revolving Credit Facility and Mortgage Repurchase Facility, changes in interest rates generally do not affect the fair value of the outstanding borrowing on the debt facilities, but does affect our earnings and cash flows. See “**Forward-Looking Statements**” above.

**Item 4. Controls and Procedures**

(a) *Conclusion regarding the effectiveness of disclosure controls and procedures* - An evaluation of the effectiveness of the design and operation of our disclosure controls and procedures was performed under the supervision, and with the participation, of our management, including the Chief Executive Officer (principle executive officer) and the Chief Financial Officer (principal financial officer). Based on that evaluation, our management, including the Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

(b) *Changes in internal control over financial reporting* - There were no changes in our internal control over financial reporting that occurred during the quarter ended March 31, 2019 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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**M.D.C. HOLDINGS, INC.**

**FORM 10-Q**

**PART II**

**Item 1. Legal Proceedings**

Because of the nature of the homebuilding business, we and certain of our subsidiaries and affiliates have been named as defendants in various claims, complaints and other legal actions arising in the ordinary course of business, including product liability claims and claims associated with the sale and financing of our homes. In the opinion of management, the outcome of these ordinary course matters will not have a material adverse effect upon our financial condition, results of operations or cash flows.

**Item 1A. Risk Factors**

There have been no significant changes in the risk factors previously identified as being attendant to our business in our Annual Report on Form 10-K for the year ended December 31, 2018. For a more complete discussion of other risk factors that affect our business, see “Risk Factors” in our Form 10-K for the year ended December 31, 2018, which include the following:

*Changes in general economic, real estate and other business conditions may have an adverse effect on the homebuilding and mortgage industries, which could have a negative impact on our business.*

*Increased competition levels in the homebuilding and mortgage lending industries could have a negative impact on our homebuilding and mortgage operations.*

*If land is not available at reasonable prices or terms, we could be required to scale back our operations in a given market and/or we may operate at lower levels of profitability.*

*Supply shortages and other risks related to the demand for skilled labor and building materials could increase costs and delay deliveries.*



*If mortgage interest rates rise, if down payment requirements are increased, if loan limits are decreased, or if mortgage financing otherwise becomes less available, it could adversely affect our business.*

*Changes to tax laws, incentives or credits currently available to our customers may negatively impact our business.*

*A decline in the market value of our homes or carrying value of our land would have a negative impact on our business.*

*Natural disasters could cause an increase in home construction costs, as well as delays, and could negatively impact our business.*

*Changes in energy prices or regulations may have an adverse effect on our cost of building homes.*

*We have financial needs that we meet through the capital markets, including the debt and secondary mortgage markets, and disruptions in these markets could have an adverse impact on the results of our business.*

*Our business is subject to numerous federal, state and local laws and regulations concerning land development, construction of homes, sales, mortgage lending, environmental and other aspects of our business. These laws and regulations could give rise to additional liabilities or expenditures, or restrictions on our business.*

*In the ordinary course of business, we are required to obtain surety bonds, the unavailability of which could adversely affect our business.*

*Decreases in the market value of our investments in marketable securities could have an adverse impact on our business.*

*Product liability litigation and warranty claims that arise in the ordinary course of business may be costly.*

*Repurchase requirements associated with HomeAmerican's sale of mortgage loans, could negatively impact our business.*

*Because of the seasonal nature of our business, our quarterly operating results can fluctuate.*

*We are dependent on the services of key employees, and the loss of their services could hurt our business.*

*The interests of certain controlling shareholders may be adverse to other investors.*

*Information technology failures and data security breaches could harm our business.*

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The Company did not repurchase any shares during the three months ended March 31, 2019. Additionally, there were no sales of unregistered equity securities during the period.

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**Item 6. Exhibits**

- 10.1 Restricted Stock Agreement Amendment (Executive Officers) under the 2011 Equity Incentive Plan, dated as of February 6, 2019.
- 10.2 Stock Option Agreement Amendment (Executive Officers) under the 2011 Equity Incentive Plan, dated as of February 6, 2019.
- 10.3 Form of Executive Officer Restricted Stock Agreement under the 2011 Equity Incentive Plan, adopted as of March 18, 2019.
- 10.4 Form of Executive Officer Stock Option Agreement under the 2011 Equity Incentive Plan, adopted as of March 18, 2019.
- 31.1 Certification of Chief Executive Officer required by 17 CFR 240.13a-14(a), pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Chief Financial Officer required by 17 CFR 240.13a-14(a), pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Chief Executive Officer required by 17 CFR 240.13a-14(b), pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer required by 17 CFR 240.13a-14(b), pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

The following financial statements, formatted in XBRL: (i) Consolidated Balance Sheets as of March 31, 2019 and December 31, 2018, (ii) Consolidated Statements of Operations for the three months ended March 31, 2019 and 2018, (iii) Consolidated Statements of Changes in Stockholders' Equity for the three months ended March 31, 2019 and 2018, (iv) Consolidated Statements of Cash Flows for the three months ended March 31, 2019 and 2018; and (v) Notes to the Unaudited Consolidated Financial Statements, tagged as blocks of text.

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**M.D.C. HOLDINGS, INC.**

(Registrant)

Date: April 30, 2019

By: /s/ Robert N. Martin

Robert N. Martin

*Senior Vice President, Chief Financial Officer and Principal Accounting*

*Officer (principal financial officer and duly authorized officer)*