

STIFEL FINANCIAL CORP  
Form 10-Q  
August 09, 2006

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

☒ x

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

For the quarterly period ended June 30, 2006

OR

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

For the transition period from    to   

Commission file number I-9305

STIFEL FINANCIAL CORP.

(Exact name of registrant as specified in its charter)

DELAWARE

(State or other jurisdiction of incorporation or  
organization)

43-1273600

(I.R.S. Employer Identification No.)

501 N. Broadway, St. Louis, Missouri

(Address of principal executive offices)

63102-2188

(Zip Code)

Registrant's telephone number, including area code

314-342-2000

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

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No "

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

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

As of July 31, 2006, there were 11,805,316 shares of Stifel Financial Corp. common stock, par value \$0.15, outstanding.

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Stifel Financial Corp.

**Form 10-Q Index**  
**June 30, 2006**

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## PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

STIFEL FINANCIAL CORP.  
CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(In thousands, except par values and share amounts)

|                                                                                                                                                                   | <u>June 30, 2006</u><br>(Unaudited) | <u>December 31, 2005</u><br>(Audited) |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------|---------------------------------------|
| <b><u>ASSETS</u></b>                                                                                                                                              |                                     |                                       |
| Cash and cash equivalents                                                                                                                                         | \$ 21,815                           | \$ 12,529                             |
| Cash segregated under federal and other regulations                                                                                                               | 26                                  | 6                                     |
| Securities purchased under agreements to resell                                                                                                                   | 153,571                             | 65,599                                |
| Receivables from brokers and dealers:                                                                                                                             |                                     |                                       |
| Securities failed to deliver                                                                                                                                      | 14,009                              | 9,137                                 |
| Deposits paid for securities borrowed                                                                                                                             | 49,577                              | 56,278                                |
| Clearing organizations                                                                                                                                            | <u>32,050</u>                       | <u>24,553</u>                         |
|                                                                                                                                                                   | 95,636                              | 89,968                                |
| Receivables from customers, net of allowance for doubtful receivables of \$301 and \$204, respectively                                                            | 294,703                             | 259,389                               |
| Securities owned, at fair value                                                                                                                                   | 139,561                             | 105,514                               |
| Securities owned and pledged, at fair value                                                                                                                       | <u>200,205</u>                      | <u>135,211</u>                        |
|                                                                                                                                                                   | 339,766                             | 240,725                               |
| Investments                                                                                                                                                       | 50,769                              | 46,628                                |
| Membership in exchanges                                                                                                                                           | 168                                 | 275                                   |
| Office equipment and leasehold improvements, at cost, net of allowances for depreciation and amortization of \$27,938 and \$26,026, respectively                  | 12,427                              | 11,422                                |
| Goodwill and intangible assets                                                                                                                                    | 14,463                              | 13,849                                |
| Loans and advances to investment executives and other employees, net of allowance for doubtful receivables from former employees of \$664 and \$767, respectively | 22,803                              | 21,105                                |
| Deferred tax asset                                                                                                                                                | 12,672                              | 10,336                                |
| Other assets                                                                                                                                                      | <u>42,134</u>                       | <u>70,170</u>                         |
|                                                                                                                                                                   | <u>\$1,060,953</u>                  | <u>\$842,001</u>                      |
| <b>Total Assets</b>                                                                                                                                               |                                     |                                       |

**LIABILITIES AND STOCKHOLDERS' EQUITY**

Liabilities

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|                                                                                                                      |                    |                  |
|----------------------------------------------------------------------------------------------------------------------|--------------------|------------------|
| Short-term borrowings from banks                                                                                     | \$ 193,350         | \$ 141,000       |
| Drafts payable                                                                                                       | 16,908             | 29,697           |
| Payables to brokers and dealers:                                                                                     |                    |                  |
| Securities failed to receive                                                                                         | 33,931             | 8,794            |
| Deposits received from securities loaned                                                                             | 118,936            | 89,039           |
| Clearing organizations                                                                                               | <u>2,483</u>       | <u>797</u>       |
|                                                                                                                      | 155,350            | 98,630           |
| Payables to customers                                                                                                | 86,099             | 78,456           |
| Securities sold, but not yet purchased, at fair value                                                                | 241,158            | 146,914          |
| Accrued employee compensation                                                                                        | 39,695             | 35,154           |
| Accounts payable and accrued expenses                                                                                | 25,900             | 59,875           |
| Debenture to Stifel Financial Capital Trust I                                                                        | 34,500             | 34,500           |
| Debenture to Stifel Financial Capital Trust II                                                                       | 35,000             | 35,000           |
| Other                                                                                                                | <u>24,598</u>      | <u>24,598</u>    |
|                                                                                                                      | <u>852,558</u>     | <u>683,824</u>   |
| Liabilities subordinated to claims of general creditors                                                              | <u>2,955</u>       | <u>3,084</u>     |
| Stockholders' Equity                                                                                                 |                    |                  |
| Preferred stock -- \$1 par value; authorized 3,000,000 shares; none issued                                           | --                 | --               |
| Common stock -- \$0.15 par value; authorized 30,000,000 shares; issued 11,904,945 and 10,296,279 shares respectively | 1,786              | 1,161            |
| Additional paid-in capital                                                                                           | 124,110            | 75,225           |
| Retained earnings                                                                                                    | <u>83,053</u>      | <u>80,279</u>    |
|                                                                                                                      | 208,949            | 156,665          |
| Less:                                                                                                                |                    |                  |
| Treasury stock, at cost, 60,698 and 4,316 shares, respectively                                                       | 2,050              | 9                |
| Unearned employee stock ownership plan shares, at cost, 151,839 and 162,683 shares, respectively                     | <u>1,459</u>       | <u>1,563</u>     |
| Total Stockholders' Equity                                                                                           | <u>205,440</u>     | <u>155,093</u>   |
| Total Liabilities and Stockholders' Equity                                                                           | <u>\$1,060,953</u> | <u>\$842,001</u> |

See Notes to Condensed Consolidated Financial Statements (unaudited).

STIFEL FINANCIAL CORP.  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)  
(In thousands, except per share amounts)

|                                                        | <u>Three Months Ended</u><br><u>June 30,</u> |                 | <u>Six Months Ended</u><br><u>June 30,</u> |                 |
|--------------------------------------------------------|----------------------------------------------|-----------------|--------------------------------------------|-----------------|
|                                                        | <u>2006</u>                                  | <u>2005</u>     | <u>2006</u>                                | <u>2005</u>     |
| <b>REVENUES</b>                                        |                                              |                 |                                            |                 |
| Commissions                                            | \$ 48,064                                    | \$ 23,557       | \$ 96,240                                  | \$ 47,892       |
| Principal transactions                                 | 20,754                                       | 10,761          | 42,380                                     | 21,742          |
| Investment banking                                     | 15,757                                       | 15,656          | 31,505                                     | 29,397          |
| Asset management and service fees                      | 14,239                                       | 10,146          | 27,737                                     | 19,597          |
| Interest                                               | 8,635                                        | 4,318           | 15,826                                     | 7,758           |
| Other                                                  | <u>(98)</u>                                  | <u>773</u>      | <u>7,260</u>                               | <u>118</u>      |
| <b>Total revenues</b>                                  | <u>107,351</u>                               | <u>65,211</u>   | <u>220,948</u>                             | <u>126,504</u>  |
| Less: Interest expense                                 | <u>4,684</u>                                 | <u>1,240</u>    | <u>8,747</u>                               | <u>2,345</u>    |
| <b>Net revenues</b>                                    | <u>102,667</u>                               | <u>63,971</u>   | <u>212,201</u>                             | <u>124,159</u>  |
| <b>NON-INTEREST EXPENSES</b>                           |                                              |                 |                                            |                 |
| Employee compensation and benefits                     | 74,385                                       | 41,593          | 161,079                                    | 82,282          |
| Occupancy and equipment rental                         | 7,267                                        | 5,117           | 14,762                                     | 10,622          |
| Communications and office supplies                     | 6,483                                        | 2,891           | 12,896                                     | 5,452           |
| Commissions and floor brokerage                        | 1,838                                        | 994             | 3,105                                      | 1,838           |
| Other operating expenses                               | <u>8,721</u>                                 | <u>4,071</u>    | <u>15,603</u>                              | <u>7,396</u>    |
| <b>Total non-interest expenses</b>                     | <u>98,694</u>                                | <u>54,666</u>   | <u>207,445</u>                             | <u>107,590</u>  |
| <b>Income before income taxes</b>                      | 3,973                                        | 9,305           | 4,756                                      | 16,569          |
| Provision for income taxes                             | <u>1,675</u>                                 | <u>3,685</u>    | <u>1,982</u>                               | <u>6,591</u>    |
| <b>Net income</b>                                      | <u>\$ 2,298</u>                              | <u>\$ 5,620</u> | <u>\$ 2,774</u>                            | <u>\$ 9,978</u> |
| Earnings per share:                                    |                                              |                 |                                            |                 |
| Basic                                                  | \$ 0.20                                      | \$ 0.58         | \$ 0.24                                    | \$ 1.02         |
| Diluted                                                | \$ 0.16                                      | \$ 0.46         | \$ 0.20                                    | \$ 0.81         |
| Weighted average common equivalent shares outstanding: |                                              |                 |                                            |                 |
|                                                        |                                              |                 |                                            |                 |

|         |        |        |        |        |
|---------|--------|--------|--------|--------|
| Basic   | 11,729 | 9,720  | 11,485 | 9,775  |
|         | 14,132 | 12,350 | 13,835 | 12,353 |
| Diluted |        |        |        |        |

See Notes to Condensed Consolidated Financial Statements (unaudited).

STIFEL FINANCIAL CORP.  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)(In thousands)

Six Months Ended

|                                                                 | <u>June 30, 2006</u> | <u>June 30, 2005</u> |
|-----------------------------------------------------------------|----------------------|----------------------|
| <u>CASH FLOWS FROM OPERATING ACTIVITIES</u>                     |                      |                      |
| Net income                                                      | \$J,774              | \$ 9,978             |
| Non-cash items included in net income:                          |                      |                      |
| Depreciation and amortization                                   | 1,935                | 2,457                |
| Loans and advances amortization                                 | J,991                | 3,730                |
| Losses (gains) on investments                                   | (6,512)              | 966                  |
| Deferred items                                                  | (2,028)              | (446)                |
| Compensation related to the private placement                   | 9,751                | - -                  |
| Stock based compensation                                        | <u>I4,512</u>        | <u>4,351</u>         |
|                                                                 | J3,423               | 21,036               |
| Decrease (increase) in assets:                                  |                      |                      |
| Operating receivables                                           | (40,982)             | (28,266)             |
| Cash segregated for exclusive benefit of customers              | (20)                 | - -                  |
| Securities purchased under agreements to resell                 | (87,972)             | - -                  |
| Securities owned, including those pledged                       | (99,041)             | (14,614)             |
| Loans and advances to investment executives and other employees | (4,689)              | (6,642)              |
| Excess tax benefit associated with stock based awards           | (10,158)             | - -                  |
| Other assets                                                    | K7,152               | (948)                |
| Increase (decrease) in liabilities:                             |                      |                      |
| Operating payables                                              | K2,771               | 16,831               |
|                                                                 | 94,244               | 30,477               |

|                                                                                          |                  |                 |
|------------------------------------------------------------------------------------------|------------------|-----------------|
| Securities sold, but not yet purchased                                                   |                  |                 |
| Drafts payable, accrued employee compensation, and accounts payable and accrued expenses | <u>(54,378)</u>  | <u>(6,858)</u>  |
| Cash Flows From Operating Activities                                                     | <u>(109,650)</u> | <u>11,016</u>   |
| <u>CASH FLOWS FROM INVESTING ACTIVITIES</u>                                              |                  |                 |
| Proceeds from sale or maturity of other investments                                      | 12,214           | 1,028           |
| Payments for:                                                                            |                  |                 |
| Purchase of office equipment and leasehold improvements                                  | (2,641)          | (2,756)         |
| Purchase of investments                                                                  | <u>(39,736)</u>  | <u>(1,270)</u>  |
| Cash Flows From Investing Activities                                                     | <u>(163)</u>     | <u>(2,998)</u>  |
| <u>CASH FLOWS FROM FINANCING ACTIVITIES</u>                                              |                  |                 |
| Short-term borrowings, net                                                               | M2,350           | 16,750          |
| Securities loaned                                                                        | K1,592           | (10,123)        |
| Excess tax benefit associated with stock based awards                                    | I0,158           | --              |
| Issuance of stock                                                                        | I,183            | 424             |
| Proceeds from private placement                                                          | J6,306           | --              |
| Payments for:                                                                            |                  |                 |
| Purchase of stock for treasury                                                           | (2,490)          | (9,391)         |
| Reduction of subordinated debt                                                           | --               | (633)           |
| Principal payments under capital lease obligation                                        | <u>--</u>        | <u>(39)</u>     |
| Cash Flows From Financing Activities                                                     | <u>119,099</u>   | <u>(3,012)</u>  |
| Increase in cash and cash equivalents                                                    | 9,286            | 5,006           |
| Cash and cash equivalents - beginning of period                                          | <u>12,529</u>    | <u>21,145</u>   |
| Cash and Cash Equivalents - end of period                                                | <u>\$11,815</u>  | <u>\$16,151</u> |
| <u>Supplemental disclosure of cash flow information:</u>                                 |                  |                 |
| Income tax payments                                                                      | \$ 912           | \$ 9,795        |
|                                                                                          | \$ 9,071         | \$ 2,381        |

Interest payments

Schedule of non-cash investing and financing activities:

|                                 |          |          |
|---------------------------------|----------|----------|
| Employee stock ownership plan   | \$104    | \$ 105   |
| Stock units, net of forfeitures | \$05,581 | \$ 6,874 |

See Notes to Condensed Consolidated Financial Statements (unaudited).

STIFEL FINANCIAL CORP.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE A - REPORTING POLICIES

Basis of Presentation

The condensed consolidated financial statements include the accounts of Stifel Financial Corp. and its subsidiaries (collectively referred to as the "Company"). The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and six months ended June 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006. For further information, refer to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

The preparation of the condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Management considers its significant estimates, which are most susceptible to change, to be the fair value of investments, the accrual for litigation, the allowance for doubtful receivables from loans and advances to employees, and interim incentive compensation accruals. Actual results could differ from those estimates.

Where appropriate, prior periods' financial information has been reclassified to conform to the current period presentation. The reclassification primarily relates to certain fees, which had been previously recorded in other commissions and are now more appropriately reflected in principal transactions.

Comprehensive Income

The Company's comprehensive income for the three and six months ended June 30, 2006 and 2005 was equal to the Company's net income.

## Stock-Based Compensation

On January 1, 2006, the Company adopted the provisions of SFAS No. 123 (revised 2004) "Share-Based Payment," ("SFAS No. 123R"), which requires the measurement and recognition of compensation expense for all share-based payment awards made to employees and directors based on estimated fair values. The Company adopted SFAS No. 123R using the modified prospective application. Under this method, SFAS No. 123R will apply to new awards and to awards outstanding on the effective date as well as those that are subsequently modified or cancelled. Compensation expense for outstanding awards for which the requisite service had not been rendered as of the effective date will be recognized over the remaining service period using the compensation cost calculated for pro forma disclosure purposes under SFAS No. 123 "Accounting for Stock-Based Compensation" ("SFAS No. 123"). Accordingly, prior period amounts have not been restated to reflect the impact of SFAS No. 123R.

In the first half of 2006, the adoption of SFAS No. 123R resulted in incremental stock-based compensation expense of \$292,363, which caused net income to decrease by \$145,597 and basic and diluted earnings per share to decrease by \$0.01 per share. Additionally, SFAS No. 123R amends SFAS No. 95, "Statement of Cash Flows," to require the excess tax benefits to be reported as a financing cash inflow rather than a reduction of taxes paid, which is included within operating cash flows. Accordingly, cash provided by operating activities decreased and cash provided by financing activities increased by \$10,157,985 related to excess tax benefits from stock-based awards.

Prior to the adoption of SFAS No. 123R, the Company applied Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees" ("APB Opinion No. 25") to account for its stock-based awards. The following table details the effect on net income and earnings per share had compensation expense for the Employee Stock-Based Awards been recorded in the three and six months ended June 30, 2005 based on the fair value method under SFAS No. 123:

| (in thousands, except per share amounts)                                                           | <u>Three Months Ended</u><br><u>June 30, 2005</u> | <u>Six Months Ended</u><br><u>June 30, 2005</u> |
|----------------------------------------------------------------------------------------------------|---------------------------------------------------|-------------------------------------------------|
| <u>Net Income:</u>                                                                                 |                                                   |                                                 |
| As reported                                                                                        | \$M,620                                           | \$ 9,978                                        |
| Add: Stock-based employee compensation expense included in reported net income, net of related tax | J,034                                             | L,665                                           |
| Deduct: Total stock-based employee compensation expense determined under SFAS 123                  | <u>(2,330)</u>                                    | <u>(5,081)</u>                                  |
| Pro forma                                                                                          | <u>\$M,324</u>                                    | <u>\$ 9,562</u>                                 |
| <u>Basic earnings per share</u>                                                                    |                                                   |                                                 |
| :                                                                                                  |                                                   |                                                 |
| As reported                                                                                        | \$0.58                                            | \$1.02                                          |
| Pro forma                                                                                          | \$0.55                                            | \$0.98                                          |
| <u>Diluted earnings per share</u>                                                                  |                                                   |                                                 |
| :                                                                                                  |                                                   |                                                 |
| As reported                                                                                        | \$0.46                                            | \$0.81                                          |
| Pro forma                                                                                          | \$0.43                                            | \$0.77                                          |

For the Company's pro forma computation, the fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model, with the following weighted-average assumptions used for grants in the first

six months of 2005: dividend yield of 0.00%; expected volatility of 31.2%; risk-free interest rates of 3.88%; and expected lives of 5.73 years.

## Recent Accounting Pronouncements

In March 2005, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations, an interpretation of Statement of Financial Accounting Standards ("SFAS") No. 143, Accounting for Asset Retirement Obligations ("FIN 47"). FIN 47 clarifies the term conditional asset retirement obligation as used in SFAS No. 143. FIN 47 refers to a legal obligation to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. Accordingly, an entity is required to recognize a liability for the fair value of a conditional asset retirement obligation if the fair value of the liability can be reasonably estimated. The Company's adoption of FIN 47 did not have a material impact on the Company's Condensed Consolidated Financial Statements.

In June 2005, the Emerging Issues Task Force ("EITF") reached a consensus on EITF Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights" ("EITF No. 04-5"). EITF No. 04-5 consensus requires a general partner in a limited partnership to consolidate the limited partnership unless the presumption of control is overcome. The general partner may overcome this presumption of control and not consolidate the entity if the limited partners have: (a) the substantive ability to dissolve or liquidate the limited partnership or otherwise remove the general partner without having to show cause; or (b) substantive participating rights in managing the partnership. This consensus is effective for general partners of all new limited partnerships formed and for existing limited partnerships for which the partnership agreements are modified subsequent to the date of the ratification of this consensus (June 29, 2005). The adoption of EITF No. 04-5 did not have a material impact on the Company's Condensed Consolidated Financial Statements.

In June 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections - a replacement of APB Opinion No. 20 and FASB Statement No. 3," ("SFAS No. 154"). SFAS No. 154 changes the requirements for the accounting for and reporting of a change in accounting principle. The adoption of SFAS No. 154 did not have a material impact on the Company's Condensed Consolidated Financial Statements.

In June 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109* ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in a Company's financial statements and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 will be effective for the Company beginning in the first quarter of 2007. The Company is in the process of evaluating the impact of adopting FIN 48 on the Company's Condensed Consolidated Financial Statements.

## NOTE B - STOCK-BASED COMPENSATION PLANS

The Company has several stock-based compensation plans. All stock-based compensation plans are administered by the Compensation Committee of the Board of Directors of Stifel Financial Corp., which has the authority to interpret the Plans, determine to whom awards may be granted under the Plans, and determine the terms of each award.

### Stock Units

A stock unit represents the right to receive a share of common stock from the Company at a designated time in the future without cash payment by the employee and is issued in lieu of cash incentive. A deferred compensation plan is provided to certain revenue producers, officers, and key administrative employees, whereby a certain percentage of their incentive compensation is deferred as defined by the plan into Company stock units with a 25% matching contribution by the Company. Participants may elect to defer up to an additional 15% of their incentive compensation with a 25% matching contribution by the Company. Units generally vest over a three- to five-year period and are

distributable upon vesting or at future specified dates. Deferred compensation costs are amortized on a straight-line basis over the vesting period.

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During the three month period ended June 30, 2006, the Company granted 92,899 units at an average value of \$40.17 per unit and converted 16,318 units into common stock. During the six month period ended June 30, 2006, the Company granted 2,108,476 units at an average value of \$37.87 per unit and converted 825,967 units into common stock.

|                                    | Three Months ended June 30,<br>2006 |                        | Six Months ended June 30,<br>2006 |                           |
|------------------------------------|-------------------------------------|------------------------|-----------------------------------|---------------------------|
| Stock Units                        | Shares                              | Average Grant<br>Price | Shares                            | Average<br>Grant<br>Price |
| Outstanding at beginning of period | 4,130,126                           |                        | 2,943,484                         |                           |
| Granted                            | 92,899                              | \$ 40.17               | 2,108,476                         | \$37.87                   |
| Converted                          | (16,318)                            |                        | (825,967)                         |                           |
| Cancelled                          | (6,175)                             |                        | (25,461)                          |                           |
| Outstanding at end of period       | 4,200,532                           |                        | 4,200,532                         |                           |

On January 2, 2006, the Company granted 1,807,610 restricted stock units to key associates of the Legg Mason Capital Markets business ("LM Capital Markets") (See Note G). The units were granted in accordance with the Company's 2001 incentive stock award plan as amended with a grant date fair value of \$37.59 per unit. The units vest ratably over a three year period, and accordingly, the Company incurred compensation expense of \$5,736,122 in the second quarter of 2006 and \$11,253,505 for the first six months of 2006.

The total stock unit compensation cost recognized for the quarter ending June 30, 2006 and 2005 was \$8,230,392 and \$2,033,580, respectively. For the six month period ended June 30, 2006 and 2005, the total stock unit compensation cost recognized was \$16,526,120 and \$4,665,394 respectively. The total tax benefit for the three month period ended June 30, 2006 and June 30, 2005 related thereto was \$62,994 and \$18,967, respectively. For the six-month period ended June 30, 2006 and June 30, 2005 the total tax benefit related thereto was \$8,569,507 and \$1,443,327 respectively.

### Stock Option/Incentive Award Plans

The Company has four incentive stock award plans. Under the Company's 1997 and 2001 Incentive Stock Plans, the Company may grant incentive stock options, stock appreciation rights, restricted stock, performance awards, and stock units up to an aggregate of 8,748,659 shares. Options under these plans are generally granted at market value at the date of the grant and expire ten years from the date of grant. The options generally vest ratably over a three- to five-year vesting period. The Company has also granted stock options to external board members under a non-qualified plan and the "Equity Incentive Plan for Non-Employee Directors." Under the Equity Incentive Plan for Non-Employee Directors, the Company may grant stock options and stock units up to 200,000 shares. The exercise price of the option is equal to market value at the date of the grant and are exercisable six months to one year from date of grant and expire ten years from date of grant. Under the Stifel, Nicolaus & Company, Incorporated Wealth Accumulation Plan ("SWAP"), a deferred compensation plan for Investment Executives, the Company may grant stock units up to 933,333 shares.

As of June 30, 2006, there was \$1,446,615 of total unrecognized compensation cost related to non-vested option awards. That cost is expected to be recognized over a weighted average period of 2.20 years.

The summary of the status of the Company's stock option plans as of June 30, 2006 and changes during the three and six-month period is presented below:

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| Options                                                          | Three Months ended June 30, 2006 |                                 | Six Months ended June 30, 2006 |                                 |
|------------------------------------------------------------------|----------------------------------|---------------------------------|--------------------------------|---------------------------------|
|                                                                  | Shares                           | Weighted Average Exercise Price | Shares                         | Weighted Average Exercise Price |
| Outstanding at beginning of period                               | 1,589,194                        | \$ 10.15                        | 1,665,363                      | \$ 9.95                         |
| Granted                                                          | - -                              | - -                             | 8,000                          | \$38.25                         |
| Exercised                                                        | (54,618)                         | \$ 8.45                         | (138,787)                      | \$ 8.71                         |
| Cancelled                                                        | - -                              | - -                             | - -                            | - -                             |
| Outstanding at end of period                                     | 1,534,576                        | \$ 10.21                        | 1,534,576                      | \$ 10.21                        |
| Options exercisable                                              | 1,209,239                        | \$ 8.81                         | 1,209,239                      | \$ 8.81                         |
| Weighted-average fair value of options granted during the period | n/a                              |                                 | \$14.58                        |                                 |

The total intrinsic value of options exercised during the three and six-month periods ended June 30, 2006 was \$1,649,067 and \$4,050,175, respectively. For the three and six-month periods ended June 30, 2005, the total intrinsic value of options exercised was \$532,732 and \$938,269, respectively. The total fair value of options vested during the three and six-month period ended June 30, 2006 was \$514,405 and \$3,991,990, respectively.

The following table summarizes information about stock options outstanding at June 30, 2006:

| Range of Exercise Price | Options Outstanding |                                             |                                 | Options Exercisable |                                 |  |
|-------------------------|---------------------|---------------------------------------------|---------------------------------|---------------------|---------------------------------|--|
|                         | Number Outstanding  | Weighted-Average Remaining Contractual Life | Weighted-Average Exercise Price | Number Exercisable  | Weighted-Average Exercise Price |  |
| \$4.70 - \$7.41         | 221,294             | 2.66                                        | \$ 7.03                         | 221,294             | \$ 7.03                         |  |
| O.46 - O.80             | 258,509             | 4.89                                        | 7.74                            | 224,920             | 7.73                            |  |
| O.83 - 8.12             | 252,452             | 3.18                                        | 7.95                            | 239,397             | 7.95                            |  |
| 8.16 - 8.69             | 329,312             | 5.61                                        | 8.48                            | 251,882             | 8.45                            |  |
| 8.70 - I1.48            | 234,715             | 3.98                                        | 9.67                            | 187,423             | 9.69                            |  |
| I3.89 - J2.23           | 195,086             | 8.06                                        | 17.48                           | 84,323              | 17.88                           |  |
| J2.23 - K8.25           | 43,208              | 9.50                                        | 37.71                           | -                   | 0.00                            |  |
|                         | 1,534,576           | 4.83                                        | \$ 10.21                        | 1,209,239           | \$ 8.81                         |  |
| \$4.70 - \$38.25        |                     |                                             |                                 |                     |                                 |  |

The fair value of each option award is estimated on the date of grant using the Black-Scholes option valuation model that uses the assumptions noted in the following table:

|                                 |      |       |
|---------------------------------|------|-------|
| Risk-free interest rate         | 4.55 | %     |
| Expected option life            | 5.35 | Years |
| Expected stock price volatility | 32.6 | %     |
| Dividend yield                  | 0    | %     |

The risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant. The expected life (estimated period of time outstanding) of options granted was estimated using the historical exercise behavior of employees. The expected volatility was based on historical volatility for a period equal to the stock option's expected life.

The total option compensation cost recognized for the three and six-month periods ended June 30, 2006 was \$130,282 and \$292,363, respectively. There was no compensation costs recognized during the same periods ending June 30, 2005. The Company received \$461,712 and \$1,209,455 cash from the exercise of stock options during the three and six-month periods ended June 30, 2006, respectively. For the three and six-month periods ended June 30, 2005, the Company received \$344,681 and \$702,491 respectively, from the exercise of stock options. The total tax benefit for the three and six-month period ended June 30, 2006 related thereto was \$646,764 and \$1,588,479, respectively. The total tax benefit for the three and six-month period ended June 30, 2005 related thereto was \$208,059 and \$418,038 respectively.

#### NOTE C - NET CAPITAL REQUIREMENT

The Company's principal subsidiary, Stifel, Nicolaus & Company, Incorporated ("SN & Co.") is subject to the Uniform Net Capital Rule, Rule 15c3-1 under the Exchange Act (the "Rule"), which requires the maintenance of minimum net capital, as defined. SN & Co. has elected to use the alternative method permitted by the Rule that requires maintenance of minimum net capital equal to the greater of \$250,000 or 2% of aggregate debit items arising from customer transactions, as defined. The Rule also provides that equity capital may not be withdrawn or cash dividends paid if resulting net capital would be less than 5% of aggregate debit items. Another subsidiary, Century Securities Associates, Inc. ("CSA"), is also subject to minimum capital requirements that may restrict the payment of cash dividends and advances to the Company. CSA has consistently operated in excess of their capital adequacy requirements. The only restriction with regard to the payment of cash dividends by the Company is its ability to obtain cash through dividends and advances from its subsidiaries, if needed.

At June 30, 2006, SN & Co. had net capital of \$104,437,309, which was 32.00% of its aggregate debit items, and \$97,886,688 in excess of the minimum required net capital. CSA had net capital of \$3,047,035 which was \$2,881,920 in excess of minimum required net capital.

The Company's international subsidiary, Stifel Nicolaus Limited, is subject to the regulatory supervision and requirements of the Financial Services Authority ("FSA") in the United Kingdom. The FSA also has the power to set minimum capital requirements, which Stifel Nicolaus Limited has met.

#### NOTE D - LEGAL PROCEEDINGS

The Company is named in and subject to various proceedings and claims incidental to its securities business activities, including lawsuits, arbitration claims and regulatory matters. While the ultimate outcome of pending litigation, claims and regulatory matters cannot be predicted with certainty, based upon information currently known, management believes that resolution of all such matters will not have a material adverse effect on the condensed consolidated financial condition of the Company but could be material to its operating results in one or more future periods. It is reasonably possible that certain of these lawsuits, arbitrations, claims and regulatory matters could be resolved in the next year and management does not believe such resolutions will result in losses materially in excess of the amounts previously provided.

## NOTE E - SEGMENT REPORTING

The Company's reportable segments include the Private Client Group, Equity Capital Markets, Fixed Income Capital Markets, and Other. The Private Client Group segment includes branch offices and independent contractor offices of the Company's broker-dealer subsidiaries located throughout the U.S., primarily in the Midwest. These branches provide securities brokerage services, including the sale of equities, mutual funds, fixed income products, and insurance, to their private clients. The Equity Capital Markets segment includes corporate finance management and participation in underwritings (exclusive of sales credits, which are included in the Private Client Group segment), mergers and acquisitions, institutional sales, trading, research, and market making. The Fixed Income Capital Markets segment includes public finance, institutional sales and competitive underwriting, and trading. The "Other" segment includes clearing revenue, interest income from stock borrow activities, unallocated interest expense, interest income and gains and losses from investments held, and all unallocated overhead cost associated with the execution of orders; processing of securities transactions; custody of client securities; receipt, identification, and delivery of funds and securities; compliance with regulatory and legal requirements; internal financial accounting and controls; acquisition charges related to the LM Capital Markets acquisition; and general administration.

Intersegment net revenues and charges are eliminated between segments. The Company evaluates the performance of its segments and allocates resources to them based on various factors, including prospects for growth, return on investment, and return on revenues.

The Company has moved certain portions of revenues and expenses from the Fixed Income Capital Markets Segment to the Private Client Group Segment to more appropriately reflect how management evaluates the business. Prior period amounts have been reclassified to conform to the current period presentation.

Information concerning operations in these segments of business is as follows:

| (in thousands)                    | <u>Three Months Ended June 30,</u> |                        | <u>Six Months Ended June 30,</u> |                         |
|-----------------------------------|------------------------------------|------------------------|----------------------------------|-------------------------|
| <u>Net Revenues</u>               | <u>2006</u>                        | <u>2005</u>            | <u>2006</u>                      | <u>2005</u>             |
| Private Client Group              | \$M4,942                           | \$L8,452               | \$111,000                        | \$ 95,796               |
| Equity Capital Markets            | 35,311                             | 9,354                  | 69,109                           | 17,968                  |
| Fixed Income Capital Markets      | 10,636                             | 4,404                  | 22,105                           | 8,314                   |
| Other                             | <u>1,778</u>                       | <u>1,761</u>           | <u>9,987</u>                     | <u>2,081</u>            |
| <b>Total Net Revenues</b>         | <b><u>\$ 102,667</u></b>           | <b><u>\$N3,971</u></b> | <b><u>\$ 212,201</u></b>         | <b><u>\$124,159</u></b> |
| <u>Operating Contribution</u>     |                                    |                        |                                  |                         |
| Private Client Group              | \$11,690                           | \$ 11,413              | \$J4,125                         | \$ 22,471               |
| Equity Capital Markets            | 7,932                              | 3,322                  | 15,434                           | 6,052                   |
| Fixed Income Capital Markets      | 1,028                              | 1,043                  | 2,748                            | 1,714                   |
| Other/ Unallocated Overhead       | <u>(16,677)</u>                    | <u>(6,473)</u>         | <u>(37,551)</u>                  | <u>(13,668)</u>         |
|                                   | <u>\$ 3,973</u>                    | <u>\$ 9,305</u>        | <u>\$ 4,756</u>                  | <u>\$ 16,569</u>        |
| <b>Income before income taxes</b> |                                    |                        |                                  |                         |

NOTE F - STOCKHOLDERS' EQUITY AND EARNINGS PER SHARE ("EPS")

The Company has an ongoing authorization, as amended, from the Board of Directors to repurchase its common stock in the open market or in negotiated transactions in order to meet obligations under the Company's employee benefit plans and for general corporate purposes. In May 2005, the Company's Board of Directors authorized the repurchase of an additional 2,000,000 shares, for a total authorization to repurchase up to 3,000,000 shares. During the first six months of 2006, the Company repurchased 73,634 shares of its common stock, at an average price of \$33.81 per share. The Company reissued 17,252 shares of common stock and issued 1,608,666 new shares for its employee benefit plans in the first six months of 2006.

On January 23, 2006, the Company completed its private placement of 1,052,220 shares of its common stock at \$25.00 per share. The shares were purchased by key associates of the LM Capital Markets business. The Company is required to charge to compensation the difference of \$25.00 per share and the grant date fair value, as determined in accordance with SFAS No. 123R, of \$34.27 per share. As a result, the Company incurred a compensation charge of \$9,750,818 in January 2006.

Basic EPS is calculated by dividing net income by the weighted-average number of common shares outstanding. Diluted EPS is similar to basic EPS but adjusts for the effect of potential common shares.

The components of the basic and diluted EPS calculations for the three and six months ended June 30 are as follows:

Three Months Ended

June 30,

Six Months Ended

June 30

,

(in thousands, except per share amounts)

2006

2005

2006

2005

Income Available to Common Stockholders

Net Income

\$ 2,298

\$ 5,620

|                                                           |                 |
|-----------------------------------------------------------|-----------------|
|                                                           | <u>\$ 2,774</u> |
|                                                           | <u>\$ 9,978</u> |
| <u>Weighted Average Shares Outstanding</u>                |                 |
| Basic Weighted Average Shares Outstanding                 |                 |
|                                                           | 11,729          |
|                                                           | 9,720           |
|                                                           | 11,485          |
|                                                           | 9,775           |
| Effect of dilutive securities from employee benefit plans |                 |
|                                                           | <u>2,403</u>    |
|                                                           | <u>2,630</u>    |
|                                                           | <u>2,350</u>    |
|                                                           | <u>2,578</u>    |
| Diluted Weighted Average Shares Outstanding               |                 |
|                                                           | <u>14,132</u>   |
|                                                           | <u>12,350</u>   |
|                                                           | <u>13,835</u>   |
|                                                           | <u>12,353</u>   |
| Basic Earnings per share                                  |                 |
|                                                           | \$ 0.20         |
|                                                           | \$ 0.58         |
|                                                           | \$ 0.24         |
|                                                           | \$ 1.02         |
| Diluted Earnings per share                                |                 |
|                                                           | \$ 0.16         |

\$ 0.46

\$ 0.20

\$ 0.81

## NOTE G - ACQUISITION

On December 1, 2005, the Company closed on the acquisition of the LM Capital Markets, from Citigroup Inc. The LM Capital Markets business was part of Legg Mason Wood Walker, Inc. ("LMWW"), which Citigroup Inc. acquired from Legg Mason, Inc. in a substantially simultaneous closing. The LM Capital Markets business acquired by the Company includes the Investment Banking, Equity and Fixed Income Research, Equity Sales and Trading, and Taxable Fixed Income Sales and Trading Departments of LMWW and employed 429 professional and support staff who became employees of the Company on December 1, 2005. The acquisition was made to grow the Company's business and in particular the Company's Capital Markets business leveraging the skill set of the Legg Mason Capital Markets associates. Under the terms of the agreement, the Company paid Citigroup Inc. an amount equal to the net book value of assets being acquired of \$12,178,198 plus a premium of \$7,000,000 paid in cash at closing with the balance of up to an additional \$30,000,000 in potential earn-out payment by the Company to Citigroup Inc., based on the performance of the combined capital markets business of both the Company's pre-closing Fixed Income and Equity Capital Markets business and Legg Mason Capital Markets for calendar years 2006, 2007, and 2008. Such payments, if any, will be accounted for as additional purchase price.

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The following is unaudited pro forma financial data for the combined operations, assuming the transaction had taken place on January 1, 2005.

|                                                | Three Months Ended June<br>30, 2005 | Six Months Ended June<br>30, 2005 |
|------------------------------------------------|-------------------------------------|-----------------------------------|
| Total revenues                                 | \$113,886,075                       | \$243,717,930                     |
| Net income                                     | \$ 7,121,493                        | \$ 14,014,412                     |
| Diluted earnings per share                     | \$0.53                              | \$1.02                            |
| Diluted weighted average shares<br>outstanding | 13,553,000                          | 13,705,720                        |

The above pro forma data excludes reductions of certain administrative allocations by Legg Mason which as a result of synergies of the combined operations, management believes, will be significantly reduced. In addition, for the three and six months ended June 30, 2006 the Company included compensation expense of \$5,379,221 and \$20,509,261, respectively associated with the issuance of restricted stock units and the discounted offering price on its private placement respectively to key associates of the LM Capital Markets. These results do not purport to be indicative of the results which actually would have occurred.

A summary of the fair values of the net assets acquired as of December 1, 2005, based upon the current valuation estimate, is as follows:

|                           |                   |
|---------------------------|-------------------|
| Cash                      | \$324,930         |
| Investments               | 12,275,536        |
| Furniture & fixtures      | 1,542,267         |
| Accounts receivables      | K5,122,667        |
| Prepaid expenses          | N23,326           |
| Goodwill                  | 0,928,842         |
| Intangible assets         | <u>1,255,000</u>  |
| Total assets acquired     | N0,072,568        |
| Accounts payables         | J,642,748         |
| Accrued expenses          | <u>K5,025,441</u> |
| Total liabilities assumed | K7,668,189        |
| Net assets acquired       | \$22,404,379      |

The goodwill and intangible assets of \$10,183,842 were assigned to the Equity Capital Markets and Fixed Income Capital Markets in the amounts of \$8,147,074 and \$2,036,768, respectively. The total amount of goodwill and intangible assets of \$10,183,842 is expected to be deductible for tax purposes.

## NOTE H - GOODWILL AND INTANGIBLE ASSETS

The carrying amount of goodwill and intangible assets attributable to each of the Company's reportable segments is presented in the following table:

|                                      | Private<br>Client<br>Group | Equity<br>Capital<br>Markets | Fixed Income<br>Capital Markets | Total        |
|--------------------------------------|----------------------------|------------------------------|---------------------------------|--------------|
| <u>Goodwill</u>                      |                            |                              |                                 |              |
| Balance at December 31, 2005         | \$454,508                  | \$1,675,899                  | \$1,179,834                     | \$3,310,241  |
| Additions                            | --                         | N00,202                      | 150,051                         | O50,253      |
| Transfers                            | --                         | M,742,871                    | I,435,718                       | O,178,589    |
| Impairment losses                    | --                         | --                           | --                              | --           |
| Balance at June 30, 2006             | L54,508                    | 8,018,972                    | J,765,603                       | I1,239,083   |
| <u>Intangible Assets</u>             |                            |                              |                                 |              |
| Balance at December 31, 2005         | M66,384                    | 8,085,384                    | I,887,383                       | I0,539,151   |
| Additions                            | I49,000                    | I16,667                      | --                              | J65,667      |
| Transfers                            | --                         | (5,742,871)                  | (1,435,718)                     | (7,178,589)  |
| Amortization of intangible assets    | (95,024)                   | (289,822)                    | (17,500)                        | (402,346)    |
| Impairment losses                    | --                         | --                           | --                              | --           |
| Balance at June 30, 2006             | N20,360                    | J,169,358                    | L34,165                         | K,223,883    |
| Total Goodwill and intangible assets | \$1,074,868                | \$10,188,330                 | \$3,199,768                     | \$14,462,966 |

At June 30, 2006, intangible assets consisted of \$2,788,134 for customer list and \$435,749 for non-compete notes.

## NOTE I - IMPACT OF THE NYSE/ARCHIPELAGO MERGER

On March 7, 2006, the New York Stock Exchange ("NYSE") and Archipelago Holdings Inc. ("Archipelago") completed the combination of their businesses through a series of mergers into a new holding company, NYSE Group, Inc. ("NYSE Group"). Shares of NYSE Group common stock were listed on the NYSE under the ticker symbol "NYX" and commenced trading on March 8, 2006. As a result of the merger, the Company received \$370,640 in cash, and 80,177 shares of NYSE Group common stock for its NYSE seat membership. The shares are subject to certain transfer restrictions that expire ratably over a three-year period, unless the NYSE Group board of directors elects to remove or reduce the restrictions. The Company recorded a gain of \$4,870,445 which is included in Other revenues in the Condensed Consolidated Statement of Operations for the six months ended June 30, 2006. The gain was impacted by a valuation adjustment for the transfer restrictions on the shares received. Subsequent gains and losses will be recorded as the share price of NYSE Group stock fluctuates and the transfer restrictions lapse.

On May 5, 2006, the Company sold 51,900 shares of NYSE Group through a secondary public offering. The Company received cash proceeds of \$3,127,763 or \$60.27 per share which represented the fixed offering price.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

The Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements within the meaning of federal securities laws. Words such as "anticipates," "estimates," "believes," "expects" and similar expressions or words are intended to identify forward-looking statements made on behalf of the Company. Actual results are subject to risks and uncertainties, including both those specific to the Company, and in particular any potential benefit to Stifel from acquiring the Legg Mason Capital Markets ("LM Capital Markets") business, including its ability to capitalize on the relationships that benefited the LM Capital Markets business, as well as statements relating to Stifel's ability to integrate the personnel and operations, and those specific to the industry, which could cause results to differ materially from those contemplated. The risks and uncertainties include, but are not limited to, general economic conditions, actions of competitors, regulatory actions, changes in legislation and technology changes and other risks and uncertainties set forth in reports and other documents filed with the United States Securities and Exchange Commission ("SEC") from time to time. Undue reliance should not be placed on the forward-looking statements, which speak only as of the date of this Quarterly Report. The Company does not undertake any obligation to publicly update any forward-looking statements.

Critical Accounting Policies and Estimates

For a description of critical accounting policies and estimates, including those that involve varying degrees of judgment, see "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Company's Annual Report on Form 10-K for the year ended December 31, 2005. In addition, see Note A of Notes to Condensed Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005 for a more comprehensive listing of significant accounting policies.

In addition to those estimates referred to above, the Company's employee compensation and benefit expense for interim periods is impacted by estimates and assumptions. A substantial portion of the Company's employee compensation and benefits expense represents discretionary bonuses, generally determined and paid at year-end. The Company estimates the interim periods' discretionary bonus expenses based upon individual departmental profitability and total Company pre-tax profits and accrues accordingly.

Business & Economic Environment

Investor confidence in the equity markets continues to be constrained by inflation, increasing energy costs and rising interest rates. The Federal Reserve Board increased the federal funds rate by 100 basis points since December 31, 2005, and 200 basis points since June 30, 2005 to 5.25%.

The key indicators of the markets' performances, the Dow Jones Industrial Average ("DJIA"), the Standard and Poor's 500 Index ("S&P 500") and the NASDAQ composite improved from the same period last year. At June 30, 2006, the DJIA, the NASDAQ and the S&P 500 increased 9%, 6%, and 7% respectively, over their June 30, 2005 closing prices. The DJIA and S&P increased 4% and 2% respectively from their December 31, 2005 closing prices, but the NASDAQ decreased 2% from its December 31, 2005 closing. While the DJIA and S&P improved during the first half of 2006, the DJIA remains relatively unchanged from its March 31, 2006 closing price and the S&P and NASDAQ have decreased 2% and 7% respectively from their March 31, 2006 closing. With the volatility of the major market indices and the uncertainty of the magnitude of the aforementioned threats remaining, the recent results of the first half may not be indicative of future results.

## Results of Operations for the Company

Six months ended June 2006 as compared to six months ended June 2005

|                                        | June-06          |                          |                          | June-05          |                          |
|----------------------------------------|------------------|--------------------------|--------------------------|------------------|--------------------------|
| (In thousands)                         | <u>\$ Amount</u> | <u>% of Net Revenues</u> | <u>% Incr. / (Decr.)</u> | <u>\$ Amount</u> | <u>% of Net Revenues</u> |
| Revenues:                              |                  |                          |                          |                  |                          |
| Commissions and principal transactions | \$ 138,620       | 65.3%                    | 99%                      | \$ 69,634        | 56.1%                    |
| Investment banking                     | 31,505           | 14.8%                    | 7%                       | 29,397           | 23.7%                    |
| Asset management and service fees      | 27,737           | 13.1%                    | 42%                      | 19,597           | 15.8%                    |
| Interest                               | 15,826           | 7.5%                     | 104%                     | 7,758            | 6.2%                     |
| Other                                  | <u>7,260</u>     | 3.4%                     | 6,053%                   | <u>118</u>       | 0.1%                     |
| Total Revenues                         | 220,948          | 104.1%                   | 75%                      | 126,504          | 101.9%                   |
| Less: Interest expense                 | <u>8,747</u>     | 4.1%                     | 273%                     | <u>2,345</u>     | 1.9%                     |
| Net Revenues                           | 212,201          | 100.0%                   | 71%                      | 124,159          | 100.0%                   |
| Non-interest expenses:                 |                  |                          |                          |                  |                          |
| Employee compensation and benefits     | 161,079          | 75.9%                    | 96%                      | 82,282           | 66.3%                    |
| Occupancy and equipment rental         | 14,762           | 7.0%                     | 39%                      | 10,622           | 8.6%                     |
| Communications and office supplies     | 12,896           | 6.1%                     | 137%                     | 5,452            | 4.4%                     |
| Commissions and floor brokerage        | 3,105            | 1.5%                     | 69%                      | 1,838            | 1.5%                     |
| Other operating expenses               | <u>15,603</u>    | 7.3%                     | 111%                     | <u>7,396</u>     | 5.9%                     |
| Total Non-interest expenses            | 207,445          | 97.8%                    | 93%                      | 107,590          | 86.7%                    |
| Income before income taxes             | 4,756            | 2.2%                     | -71%                     | 16,569           | 13.3%                    |
| Provision for Income Taxes             | <u>1,982</u>     | 0.9%                     | -70%                     | <u>6,591</u>     | 5.3%                     |
| Net Income                             | \$2,774          | 1.3%                     | -72%                     | \$ 9,978         | 8.0%                     |

Year to date comparisons were impacted by the LM Capital Markets acquisition on December 1, 2005. As a result of the acquisition of the LM Capital Markets business, the Company added 429 employees and 22 offices on December 1, 2005. Except as noted in the following discussion of year-to date and quarterly variances for the total Company and the ensuing segment results, the underlying reasons for the increase in revenue and expense categories can be attributed principally to the acquisition.

The Company recorded net income of \$2.8 million, or \$0.20 per diluted share on net revenues of \$212.2 million for the six months ended June 30, 2006 compared to net income of \$10.0 million, or \$0.81 per diluted share, on net revenues of \$124.2 million for the same period one year earlier.

Investment banking revenues increased 7% to \$31.5 million due principally to an increase of \$15.1 million in corporate finance advisory fees offset by a decrease in corporate finance underwriting fee revenue resulting from a decreased banking calendar for lead or co-managed offerings (See Results of Operations for Equity Capital Markets).

Asset management and service fees increased 42% to \$27.7 million primarily as a result of the increase in value of assets under management and increased number of accounts (See Results of Operations for Private Client Group).

Other revenues increased \$7.1 million principally as a result of an increase in net gains on investments, primarily from the gain recorded on the NYSE seat membership (See Note I of Notes to Condensed Consolidated Financial Statements).

Interest revenue increased 104% to \$15.8 million as a result of increased revenue on fixed income inventory held for sale to clients, increased revenue from stock borrow activities and increased revenue on customer margin accounts which resulted from a 32% increase in the weighted average rates charged to those customers. Interest expense increased 273% as a result of increased costs to carry higher levels of firm inventory, interest on Stifel Financial Capital Trust II issued in August 2005, and increased rates charged for bank borrowings and stock loans to finance customer borrowings. Weighted average effective external rates increased 104% to 5.11% from 2.50% in the prior year.

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Employee compensation and benefits, which represent 76% of the Company's net revenues, increased 96% to \$161.1 million. Employee compensation and benefits was impacted by acquisition related charges of \$25.3 million, principally stock based compensation. The remaining increase was attributed to the increase in variable compensation commensurate with the increase in revenues.

Three months ended June 2006 as compared to three months ended June 2005

| (In thousands)                         | June-06          |                          |                          | June-05          |                          |
|----------------------------------------|------------------|--------------------------|--------------------------|------------------|--------------------------|
|                                        | <u>\$ Amount</u> | <u>% of Net Revenues</u> | <u>% Incr. / (Decr.)</u> | <u>\$ Amount</u> | <u>% of Net Revenues</u> |
| Revenues:                              |                  |                          |                          |                  |                          |
| Commissions and principal transactions | \$ 68,818        | 67.0%                    | 101%                     | \$ 34,318        | 53.7%                    |
| Investment banking                     | 15,757           | 15.3%                    | 1%                       | 15,656           | 24.5%                    |
| Asset management and service fees      | 14,239           | 13.9%                    | 40%                      | 10,146           | 15.9%                    |
| Interest                               | 8,635            | 8.5%                     | 100%                     | 4,318            | 6.7%                     |
| Other                                  | <u>(98)</u>      | -0.1%                    | n/a                      | <u>773</u>       | 1.1%                     |
| Total Revenues                         | 107,351          | 104.6%                   | 65%                      | 65,211           | 101.9%                   |
| Less: Interest expense                 | <u>4,684</u>     | 4.6%                     | 278%                     | <u>1,240</u>     | 1.9%                     |
| Net Revenues                           | 102,667          | 100.0%                   | 60%                      | 63,971           | 100.0%                   |
| Non-interest expenses:                 |                  |                          |                          |                  |                          |
| Employee compensation and benefits     | 74,385           | 72.5%                    | 79%                      | 41,593           | 65.0%                    |
| Occupancy and equipment rental         | 7,267            | 7.1%                     | 42%                      | 5,117            | 8.0%                     |
| Communications and office supplies     | 6,483            | 6.3%                     | 124%                     | 2,891            | 4.5%                     |
| Commissions and floor brokerage        | 1,838            | 1.8%                     | 85%                      | 994              | 1.6%                     |
| Other operating expenses               | <u>8,721</u>     | 8.4%                     | 114%                     | <u>4,071</u>     | 6.4%                     |
| Total Non-interest expenses            | 98,694           | 96.1%                    | 81%                      | 54,666           | 85.5%                    |
| Income before income taxes             | 3,973            | 3.9%                     | -57%                     | 9,305            | 14.5%                    |
| Provision for Income Taxes             | <u>1,675</u>     | 1.6%                     | -55%                     | <u>3,685</u>     | 5.7%                     |
|                                        | \$ 2,298         | 2.3%                     | -59%                     | \$ 5,620         | 8.8%                     |

Net Income

Except as noted in the following discussion of variances for the total Company and the ensuing segment results, the underlying reasons for the three month variances to the prior period are substantially the same as the comparative six month discussion and the statements contained in that discussion also apply for the three month discussion.

The Company recorded net income of \$2.3 million, or \$0.16 per diluted share on net revenues of \$102.7 million for the three months ended June 30, 2006 compared to net income of \$5.6 million, or \$0.46 per diluted share, on net revenues of \$64.0 million for the same period one year earlier.

Other revenues decreased \$871,400 principally as a result of an increase in net losses on investments.

Employee compensation and benefits, which represent 73% of the Company's net revenues, increased 79% to \$74.4 million. Employee compensation and benefits was impacted by acquisition related charges of \$7.8 million, principally stock based compensation. The remaining increase was attributed to the increase in variable compensation commensurate with the increase in revenues.

# Core Earnings for the three and six months ended June 2006

Net income for the three and six months ended June 30, 2006 was impacted by acquisition related costs, primarily stock based compensation, of \$8.3 million or \$0.34 per diluted share and \$26.1 million or \$1.11 per diluted share respectively, associated with the acquisition of the LM Capital Markets business from Citigroup Inc.

As a result of the acquisition, the Company reports Core Earnings; a non-Generally Accepted Accounting Principle ("GAAP") financial measure. Core Earnings represents GAAP net income before acquisition related charges, principally compensation expense recorded for stock based awards offered to key associates of LM Capital Markets and accounted for under Statement of Accounting Standards No. 123 (Revised 2004) "Share-Based Payment" ("SFAS No. 123R"). Management believes the supplemental disclosure of Core Earnings helps investors, rating agencies, and financial analysts better understand the performance of their business and enhances the comparison of their performance from period to period. Management uses Core Earnings to evaluate the performance of their business. Core Earnings should not be considered an alternative to any measure of performance as promulgated under GAAP (such as net income), nor should this data be considered an indicator of our overall financial performance or liquidity. Also, the calculation of Core Earnings used by the Company may not be comparable to similarly titled measures reported by other companies.

A reconciliation of Core Earnings to Net Income, and Core Earnings per Basic and Diluted Share to Net Income per Basic and Diluted Share, the most directly comparable measure under GAAP, is included in the table below.

|                                          | Three Months Ended |            | Six Months Ended |            |
|------------------------------------------|--------------------|------------|------------------|------------|
|                                          | 06/30/2006         | 06/30/2005 | 06/30/2006       | 06/30/2005 |
| GAAP Net Income                          | \$ 2,298           | \$ 5,620   | \$ 2,774         | \$ 9,978   |
| Acquisition related revenues, net of tax | 84                 |            | 89               | --         |
| Acquisition related charges, net of tax  |                    |            |                  |            |
| Private placement compensation           | --                 | --         | 5,689            | --         |
| Acquisition related compensation         | 4,334              | --         | 9,052            | --         |
| Other non-compensation charges           | <u>282</u>         | --         | <u>498</u>       | --         |
| Core Earnings                            |                    |            |                  |            |
| (1)                                      | \$ 6,998           | \$ 5,620   | \$ 18,102        | \$ 9,978   |
| Earnings per Share:                      |                    |            |                  |            |
| GAAP Earnings Per Basic Share            | \$ 0.20            | \$ 0.58    | \$ 0.24          | \$ 1.02    |
| Acquisition related charges              | <u>0.40</u>        | --         | <u>1.34</u>      | --         |
| Core Earnings Per Basic Share            | \$ 0.60            | \$ 0.58    | \$ 1.58          | \$ 1.02    |
| GAAP Earnings Per Diluted Share          | \$ 0.16            | \$ 0.46    | \$ 0.20          | \$ 0.81    |
| Acquisition related charges              | <u>0.34</u>        | --         | <u>1.11</u>      | --         |

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|                                 |         |         |         |         |
|---------------------------------|---------|---------|---------|---------|
| Core Earnings Per Diluted Share | \$ 0.50 | \$ 0.46 | \$ 1.31 | \$ 0.81 |
|---------------------------------|---------|---------|---------|---------|

<sup>(1)</sup> Core Earnings for the three and six months ended June 30, 2006 were \$7.0 million or \$0.50 per diluted share and \$18.1 million or \$1.31 per diluted share respectively. Included in the three and six months Core Earnings is (\$0.01) and \$0.16 per diluted share for the gain resulting from the merger of the New York Stock Exchange and Archipelago Holdings Inc. as a result of the subsequent market adjustment.

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## Segments Analysis

The Company's reportable segments include the Private Client Group, Equity Capital Markets, Fixed Income Capital Markets, and Other. Prior years' financial information has been reclassified to conform with the current year presentation. The Private Client Group ("PCG") segment includes branch offices and independent contractor offices of the Company's broker-dealer subsidiaries located throughout the U.S., primarily in the Midwest. These branches provide securities brokerage services, including the sale of equities, mutual funds, fixed income products, and insurance, to their private clients. The Equity Capital Markets ("ECM") segment includes corporate finance management and participation in underwritings (exclusive of sales credits, which are included in the Private Client Group segment), mergers and acquisitions, institutional sales, trading, research, and market making. The Fixed Income Capital Markets ("FICM") segment includes public finance, institutional sales and competitive underwriting, and trading. The "Other" segment includes clearing revenue, interest income from stock borrow activities, unallocated interest expense, interest income and gains and losses from investments held, and all unallocated overhead cost associated with the execution of orders; processing of securities transactions; custody of client securities; receipt, identification, and delivery of funds and securities; compliance with regulatory and legal requirements; internal financial accounting and controls; acquisition charges related to the LM Capital Markets business acquisition; and general administration.

The Company has moved certain portions of revenues and expenses from the Fixed Income Capital Markets Segment to the Private Client Group Segment to more appropriately reflect how management evaluates the business. Prior period amounts have been reclassified to conform to the current period presentation.

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Results of Operations for Private Client Group - Six Months

The following table presents consolidated information for the Private Client Group segment for the respective periods indicated.

|                                        | June-06          |                          |                          | June-05          |                          |
|----------------------------------------|------------------|--------------------------|--------------------------|------------------|--------------------------|
| (In thousands)                         | <u>\$ Amount</u> | <u>% of Net Revenues</u> | <u>% Incr. / (Decr.)</u> | <u>\$ Amount</u> | <u>% of Net Revenues</u> |
| Revenues:                              |                  |                          |                          |                  |                          |
| Commissions and principal transactions | \$ 75,513        | 68.0%                    | 21%                      | \$ 62,607        | 65.4%                    |
| Investment banking                     | 4,025            | 3.6%                     | -60%                     | 10,069           | 10.5%                    |
| Asset management and service fees      | 27,697           | 25.0%                    | 41%                      | 19,586           | 20.4%                    |
| Interest                               | 9,811            | 8.8%                     | 50%                      | 6,520            | 6.8%                     |
| Other                                  | <u>308</u>       | 0.3%                     | 413%                     | <u>60</u>        | 0.1%                     |
| Total Revenues                         | 117,354          | 105.7%                   | 19%                      | 98,842           | 103.2%                   |
| Less: Interest expense                 | <u>6,354</u>     | 5.7%                     | 109%                     | <u>3,046</u>     | 3.2%                     |
| Net Revenues                           | 111,000          | 100.0%                   | 16%                      | 95,796           | 100.0%                   |
| Non-interest expenses:                 |                  |                          |                          |                  |                          |
| Employee compensation and benefits     | 69,921           | 63.0%                    | 20%                      | 58,400           | 61.0%                    |
| Occupancy and equipment rental         | 6,540            | 5.9%                     | 6%                       | 6,176            | 6.4%                     |
| Communications and office supplies     | 3,642            | 3.3%                     | 9%                       | 3,355            | 3.5%                     |
| Commissions and floor brokerage        | 1,428            | 1.3%                     | 12%                      | 1,271            | 1.3%                     |
| Other operating expenses               | <u>5,344</u>     | 4.8%                     | 30%                      | <u>4,123</u>     | 4.3%                     |
| Total Non-interest expenses            | 86,875           | 78.3%                    | 18%                      | 73,325           | 76.5%                    |
| Income before income taxes             | \$ 24,125        | 21.7%                    | 7%                       | \$ 22,471        | 23.5%                    |

|                | <u>June 30, 2006</u> | <u>June 30, 2005</u> |
|----------------|----------------------|----------------------|
| Branch Offices | 97                   | 88                   |
|                | 485                  | 434                  |

## Investment Executives

180

177

## Independent Contractors

PCG net revenues increased 16% to \$111.0 million, principally due to increased commissions and principal transactions and increased asset management and service fees offset by a decrease in investment banking. Commissions and principal transactions increased due to the increase in the number of branch offices and investment executives. Investment banking decreased due to decreased selling concession for lead or co-managed transactions (See Results of Operations for Equity Capital Markets). Asset management and service fees increased principally due to increased wrap fees, resulting from of an increase in the number and value of managed accounts which increased 43% and 108% respectively.

| Assets Under Management | <u>June 30, 2006</u> | <u>March 31, 2006</u> | <u>June 30, 2005</u> | <u>March 31, 2005</u> |
|-------------------------|----------------------|-----------------------|----------------------|-----------------------|
| Value                   | \$3,322,806,000      | \$2,903,579,000       | \$1,597,656,000      | \$1,584,550,000       |
| Number of accounts      | 11,627               | 10,664                | 8,153                | 7,907                 |

Interest revenues for the PCG increased as a result of increased rates charged to customers for margin borrowings to finance trading activity. Interest expense increased as a result of increased rates from banks to finance those customer borrowings. (See net interest discussion in Results of Operations for the Company)

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Non-interest expenses increased 18% to \$86.9 million. Employee compensation and benefits increased 20% as a result of increased variable compensation which increased in conjunction with increased revenue production, and increased fixed compensation which increased due to the firm's continued expansion of the PCG. Employee compensation and benefits includes transition pay of \$5.4 million and \$4.3 million from 2006 and 2005, respectively, principally upfront notes and accelerated payouts in connection with the Company's expansion efforts.

Occupancy and equipment rental increased 6% principally as a result of increased occupancy cost due to an increase in the number of branch offices.

Communication and office supplies increased 9% due to the increase in the number of branch offices.

Commission and floor brokerage increased 12% due to increased transactions and commission revenue.

Other operating expenses increased 30% to \$5.3 million principally as a result of increased advertising and travel and promotion costs associated with the increase in branch offices.

As a result of the 16% increase in net revenues, income before income taxes for the Private Client Group increased 7% to \$24.1 million.

### Results of Operations for Private Client Group - Three Months

The following table presents consolidated information for the Private Client Group segment for the respective periods indicated.

| (In thousands)                         | June-06          |                          |                          | June-05          |                          |
|----------------------------------------|------------------|--------------------------|--------------------------|------------------|--------------------------|
|                                        | <u>\$ Amount</u> | <u>% of Net Revenues</u> | <u>% Incr. / (Decr.)</u> | <u>\$ Amount</u> | <u>% of Net Revenues</u> |
| Revenues:                              |                  |                          |                          |                  |                          |
| Commissions and principal transactions | \$ 36,897        | 67.2%                    | 21%                      | \$ 30,513        | 63.0%                    |
| Investment banking                     | 2,154            | 3.9%                     | -63%                     | 5,746            | 11.9%                    |
| Asset management and service fees      | 14,205           | 25.9%                    | 40%                      | 10,142           | 20.9%                    |
| Interest                               | 5,142            | 9.3%                     | 43%                      | 3,587            | 7.4%                     |
| Other                                  | <u>(58)</u>      | -0.1%                    | n/a                      | <u>110</u>       | 0.2%                     |
| Total Revenues                         | 58,340           | 106.2%                   | 16%                      | 50,098           | 103.4%                   |
| Less: Interest expense                 | <u>3,398</u>     | 6.2%                     | 106%                     | <u>1,646</u>     | 3.4%                     |
| Net Revenues                           | 54,942           | 100.0%                   | 13%                      | 48,452           | 100.0%                   |
| Non-interest expenses:                 |                  |                          |                          |                  |                          |
| Employee compensation and benefits     | 34,880           | 63.5%                    | 20%                      | 29,184           | 60.2%                    |

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|                                    |              |       |     |              |       |
|------------------------------------|--------------|-------|-----|--------------|-------|
| Occupancy and equipment rental     | 3,334        | 6.1%  | 12% | 2,980        | 6.2%  |
| Communications and office supplies | 1,835        | 3.3%  | 2%  | 1,801        | 3.7%  |
| Commissions and floor brokerage    | 753          | 1.4%  | 12% | 674          | 1.4%  |
| Other operating expenses           | <u>2,450</u> | 4.4%  | 2%  | <u>2,400</u> | 4.9%  |
| Total Non-interest expenses        | 43,252       | 78.7% | 17% | 37,039       | 76.4% |
| Income before income taxes         | \$ 11,690    | 21.3% | 2%  | \$ 11,413    | 23.6% |

PCG net revenues increased 13% to \$54.9 million, principally due to increased commissions and principal transactions and increased asset management and service fees offset by a decrease in investment banking.

Other revenues decreased \$168,000 principally due to losses on investments carried for the investment executive deferred compensation plan.

Non-interest expenses increased 17% to \$43.3 million. Employee compensation and benefits increased 20% as a result of increased variable compensation which increased in conjunction with increased revenue production and increased fixed compensation which increased due to the firm's continued expansion of the Private Client Group. Employee compensation and benefits includes transition pay of \$2.9 million and \$2.2 million from 2006 and 2005, respectively, principally upfront notes and accelerated payouts in connection with the Company's expansion efforts.

As a result of the 13% increase in net revenues, income before income taxes for the PCG increased 2% to \$11.7 million.

#### Results of Operations for Equity Capital Markets - Six Months

The following table presents consolidated information for the Equity Capital Markets segment for the respective periods indicated.

| (In thousands)                         | June-06          |                          |                          | June-05          |                          |
|----------------------------------------|------------------|--------------------------|--------------------------|------------------|--------------------------|
|                                        | <u>\$ Amount</u> | <u>% of Net Revenues</u> | <u>% Incr. / (Decr.)</u> | <u>\$ Amount</u> | <u>% of Net Revenues</u> |
| Revenues:                              |                  |                          |                          |                  |                          |
| Commissions and principal transactions | \$ 44,355        | 64.2%                    | 1,172%                   | \$ 3,486         | 19.4%                    |
| Investment banking                     | 24,077           | 34.8%                    | 66%                      | 14,495           | 80.7%                    |
| Other                                  | <u>807</u>       | 1.2%                     | 251%                     | <u>230</u>       | 1.3%                     |
| Total Revenues                         | 69,239           | 100.2%                   | 280%                     | 18,211           | 101.4%                   |
| Less: Interest expense                 | <u>130</u>       | 0.2%                     | -47%                     | <u>243</u>       | 1.4%                     |
| Net Revenues                           | 69,109           | 100.0%                   | 285%                     | 17,968           | 100.0%                   |
| Non-interest expenses:                 |                  |                          |                          |                  |                          |
| Employee compensation and benefits     | 38,964           | 56.4%                    | 333%                     | 9,003            | 50.1%                    |
| Occupancy and equipment rental         | 2,372            | 3.4%                     | 370%                     | 505              | 2.8%                     |
| Communications and office supplies     | 5,694            | 8.2%                     | 556%                     | 868              | 4.8%                     |
| Commissions and floor brokerage        | 1,386            | 2.0%                     | 182%                     | 492              | 2.7%                     |
| Other operating expenses               | <u>5,259</u>     | 7.7%                     | 402%                     | <u>1,048</u>     | 5.9%                     |
| Total Non-interest expenses            | 53,675           | 77.7%                    | 350%                     | 11,916           | 66.3%                    |

|                            |           |       |      |          |       |
|----------------------------|-----------|-------|------|----------|-------|
| Income before income taxes | \$ 15,434 | 22.3% | 155% | \$ 6,052 | 33.7% |
|----------------------------|-----------|-------|------|----------|-------|

ECM net revenues increased 285% to \$69.1 million, principally due to increased commissions and principal transactions and increased investment banking.

Investment banking revenue increased 66% to \$24.1 million due principally to increased advisory fees of \$14.8 million offset by decreased underwriting fee revenue resulting from decreased banking calendars for lead or co-managed offerings. As a result of the 285% increase in net revenues and the leverage in increased production, income before income taxes increased 155% to \$15.4 million.

## Results of Operations for Equity Capital Markets - Three Months

The following table presents consolidated information for the Equity Capital Markets segment for the respective periods indicated.

| (In thousands)                         | June-06          |                          |                         | June-05          |                          |
|----------------------------------------|------------------|--------------------------|-------------------------|------------------|--------------------------|
|                                        | <u>\$ Amount</u> | <u>% of Net Revenues</u> | <u>% Incr./ (Decr.)</u> | <u>\$ Amount</u> | <u>% of Net Revenues</u> |
| Revenues:                              |                  |                          |                         |                  |                          |
| Commissions and principal transactions | \$ 22,633        | 64.1%                    | 1119%                   | \$ 1,857         | 19.9%                    |
| Investment banking                     | 12,177           | 34.5 %                   | 64%                     | 7,426            | 79.4%                    |
| Other                                  | <u>576</u>       | 1.6%                     | 262%                    | <u>159</u>       | 1.6%                     |
| Total Revenues                         | 35,386           | 100.2%                   | 275%                    | 9,442            | 100.9%                   |
| Less: Interest expense                 | <u>75</u>        | 0.2%                     | -15%                    | <u>88</u>        | 0.9%                     |
| Net Revenues                           | 35,311           | 100.0%                   | 277%                    | 9,354            | 100.0%                   |
| Non-interest expenses:                 |                  |                          |                         |                  |                          |
| Employee compensation and benefits     | 19,267           | 54.6%                    | 330%                    | 4,483            | 47.9%                    |
| Occupancy and equipment rental         | 1,231            | 3.5%                     | 407%                    | 243              | 2.6%                     |
| Communications and office supplies     | 2,909            | 8.2%                     | 542%                    | 453              | 4.8%                     |
| Commissions and floor brokerage        | 871              | 2.5%                     | 219%                    | 273              | 2.9%                     |
| Other operating expenses               | <u>3,101</u>     | 8.7%                     | 435%                    | <u>580</u>       | 6.3%                     |
| Total Non-interest expenses            | 27,379           | 77.5%                    | 354%                    | 6,032            | 64.5%                    |
| Income before income taxes             | \$ 7,932         | 22.5%                    | 139%                    | \$ 3,322         | 35.5%                    |

ECM net revenues increased 277% to \$35.3 million, principally due to increased commissions and principal transactions and increased investment banking. Investment banking revenue increased principally due to increased advisory fees of \$6.5 million offset by a decrease in underwriting fees due to a decreased banking calendar for lead or co-managed offerings.

As a result of the 277% increase in net revenues and the leverage in increased production, income before income taxes increased 139% to \$7.9 million.

## Results of Operations for Fixed Income Capital Markets - Six Months

The following table presents consolidated information for the Fixed Income Capital Markets segment for the respective periods indicated.

|                                        | June-06          |                          |                          | June-05          |                          |
|----------------------------------------|------------------|--------------------------|--------------------------|------------------|--------------------------|
| (In thousands)                         | <u>\$ Amount</u> | <u>% of Net Revenues</u> | <u>% Incr. / (Decr.)</u> | <u>\$ Amount</u> | <u>% of Net Revenues</u> |
| Revenues:                              |                  |                          |                          |                  |                          |
| Commissions and principal transactions | \$ 18,752        | 84.8%                    | 432%                     | \$ 3,526         | 42.4%                    |
| Investment banking                     | 3,403            | 15.4%                    | -30%                     | 4,833            | 58.1%                    |
| Interest                               | 7,050            | 31.9%                    | 7,821%                   | 89               | 1.1%                     |
| Other                                  | <u>2</u>         | 0%                       | -78%                     | <u>2</u>         | 0.1%                     |
| Total Revenues                         | 29,207           | 132.1%                   | 245%                     | 8,457            | 101.7%                   |
| Less: Interest expense                 | 7,102            | 32.1%                    | 4,832%                   | 143              | 1.7%                     |
| Net Revenues                           | 22,105           | 100.0%                   | 166%                     | 8,314            | 100.0%                   |
| Non-interest expenses:                 |                  |                          |                          |                  |                          |
| Employee compensation and benefits     | 14,205           | 64.3%                    | 192%                     | 4,872            | 58.6%                    |
| Occupancy and equipment rental         | 1,134            | 5.1%                     | 220%                     | 354              | 4.3%                     |
| Communications and office supplies     | 1,665            | 7.5%                     | 490%                     | 282              | 3.4%                     |
| Commissions and floor brokerage        | 290              | 1.3%                     | 282%                     | 76               | 0.9%                     |
| Other operating expenses               | <u>2,063</u>     | 9.4%                     | 103%                     | <u>1,016</u>     | 12.2%                    |
| Total Non-interest expenses            | 19,357           | 87.6%                    | 193%                     | 6,600            | 79.4%                    |
| Income before income taxes             | \$ 2,748         | 12.4%                    | 60%                      | \$ 1,714         | 20.6%                    |

Net revenues for the first six months of 2006 increased 166% to \$22.1 million from the same time period last year principally due to an increase in commissions and principal transactions and interest offset by a decrease in investment banking. Investment banking revenues decreased as a result of decreased municipal refinancings resulting from increased interest rates.

As a result of the 166% increase in net revenue and the leverage in increased production, income before income taxes increased 60% to \$2.7 million.



## Results of Operations for Fixed Income Capital Markets - Three Months

The following table presents consolidated information for the Fixed Income Capital Markets segment for the respective periods indicated.

|                                        | June-06          |                          |                          | June-05          |                          |
|----------------------------------------|------------------|--------------------------|--------------------------|------------------|--------------------------|
| (In thousands)                         | <u>\$ Amount</u> | <u>% of Net Revenues</u> | <u>% Incr. / (Decr.)</u> | <u>\$ Amount</u> | <u>% of Net Revenues</u> |
| Revenues:                              |                  |                          |                          |                  |                          |
| Commissions and principal transactions | \$ 9,288         | 87.3%                    | 377%                     | \$ 1,948         | 44.2%                    |
| Investment banking                     | 1,426            | 13.4%                    | -43%                     | 2,484            | 56.4%                    |
| Interest                               | 4,729            | 44.5%                    | 8,657%                   | 54               | 1.2%                     |
| Other                                  | <u>1</u>         | 0.0%                     | -75%                     | <u>4</u>         | 0.2%                     |
| Total Revenues                         | 15,444           | 145.2%                   | 244%                     | 4,490            | 102.0%                   |
| Less: Interest expense                 | <u>4,808</u>     | 45.2%                    | 5,491%                   | <u>86</u>        | 2.0%                     |
| Net Revenues                           | 10,636           | 100.0%                   | 142%                     | 4,404            | 100.0%                   |
| Non-interest expenses:                 |                  |                          |                          |                  |                          |
| Employee compensation and benefits     | 7,006            | 65.9%                    | 184%                     | 2,469            | 56.0%                    |
| Occupancy and equipment rental         | 490              | 4.6%                     | 199%                     | 164              | 3.7%                     |
| Communications and office supplies     | 813              | 7.6%                     | 435%                     | 152              | 3.5%                     |
| Commissions and floor brokerage        | 214              | 2.0%                     | 355%                     | 47               | 1.1%                     |
| Other operating expenses               | <u>1,085</u>     | 10.2%                    | 105%                     | <u>529</u>       | 12.0%                    |
| Total Non-interest expenses            | 9,608            | 90.3%                    | 186%                     | 3,361            | 76.3%                    |
| Income before income taxes             | \$ 1,028         | 9.7%                     | -1%                      | \$ 1,043         | 23.7%                    |

Net revenues for the second quarter of 2006 increased 142% to \$10.6 million from the same time period last year principally due to an increase in commissions and principal transactions and interest offset by a decrease in investment banking.

## Results of Operations for Other Segment -Six Months

The following table presents consolidated information for the Other segment for the respective periods indicated.

|                                    | June-06          |                                    | June-05          |
|------------------------------------|------------------|------------------------------------|------------------|
| (In thousands)                     | <u>\$ Amount</u> | <u>% Incr. /</u><br><u>(Decr.)</u> | <u>\$ Amount</u> |
| Net Revenues                       | \$ 9,987         | 380%                               | \$ 2,081         |
| Non-interest expenses:             |                  |                                    |                  |
| Employee compensation and benefits | 37,989           | 280%                               | 10,007           |
| Other operating expenses           | 9,549            | 66%                                | 5,742            |
| Total Non-interest expenses        | 47,538           | 202%                               | 15,749           |
| Losses before income tax           | \$ (37,551)      | n/a                                | \$ (13,668)      |

Net revenues for the Other segment increased to \$10.0 million principally as a result of an increase in gains on investments, primarily from the previously discussed \$4.9 million gain on the NYSE membership seat. (See Note I of Notes to Condensed Consolidated Financial Statements).

Total Non-interest expenses increased due to the previously discussed acquisition charges, primarily stock-based compensation, of \$25.3 million related to the acquisition charges of the LM Capital Markets business. (See Note G of Notes to Condensed Consolidated Financial Statements).

## Results of Operations for Other Segment -Three Months

The following table presents consolidated information for the Other segment for the respective periods indicated.

|                                    | June-06          |                                    | June-05          |
|------------------------------------|------------------|------------------------------------|------------------|
| (In thousands)                     | <u>\$ Amount</u> | <u>% Incr. /</u><br><u>(Decr.)</u> | <u>\$ Amount</u> |
| Net Revenues                       | \$ 1,778         | 1%                                 | \$ 1,761         |
| Non-interest expenses:             |                  |                                    |                  |
| Employee compensation and benefits | 13,232           | 142%                               | 5,457            |
| Other operating expenses           | 5,223            | 88%                                | 2,777            |
| Total Non-interest expenses        | 18,455           | 124%                               | 8,234            |
| Losses before income tax           | \$ (16,677)      | n/a                                | \$ (6,473)       |

Net revenues for the Other segment increased 1% to \$1.8 million.

Total Non-interest expenses increased due to the previously discussed acquisition charges, primarily stock-based compensation, of \$7.8 million related to the acquisition charges of the LM Capital Markets business. (See Note G of Notes to Condensed Consolidated Financial Statements).

## Liquidity and Capital Resources

The Company's assets are principally highly liquid, consisting mainly of cash or assets readily convertible into cash. These assets are financed primarily by the Company's equity capital, debenture to Stifel Financial Capital Trust I, debenture to Stifel Financial Capital Trust II, short-term bank loans, reverse repurchase agreements, proceeds from securities lending, and other payables. Changes in securities market volumes, related customer borrowing demands, underwriting activity, and levels of securities inventory affect the amount of the Company's financing requirements.

On January 2, 2006, the Company granted 1,807,610 restricted stock units to key associates of the LM Capital Markets. The units were granted in accordance with the Company's 2001 incentive stock award plan as amended with a grant date fair value of \$37.59 per unit. The units vest ratably over a three year period, and accordingly, the Company incurred compensation expense of \$11.3 million for the six months ended June 30, 2006 respectively.

On January 23, 2006, the Company completed its private placement of 1,052,220 shares of its common stock at \$25.00 per share. The shares were purchased by key associates of the LM Capital Markets business. The Company is required to charge to compensation the difference of \$25.00 per share and the grant date fair value, as determined in accordance with SFAS No. 123R, of \$34.27 per share. As a result, the Company incurred a compensation charge of \$9.8 million in January 2006.

In the first six months of 2006, the Company purchased \$3.1 million in fixed assets, consisting primarily of information technology equipment, leasehold improvements and furniture and fixtures.

The Company has an ongoing authorization, as amended, from the Board of Directors to repurchase its common stock in the open market or in negotiated transactions in order to meet obligations under the Company's employee benefit plans and for general corporate purposes. In May 2005, the Company's Board of Directors authorized the repurchase of an additional 2,000,000 shares, for a total authorization to repurchase up to 3,000,000 shares. During the first six months of 2006, the Company repurchased 73,634 shares of its common stock, at an average price of \$33.81 per share. The Company reissued 17,252 shares of common stock and issued 1,608,666 new shares for its employee benefit plans in the first six months of 2006.

Stifel, Nicolaus & Company, Incorporated ("SN & Co."), the Company's principal broker-dealer subsidiary, and Century Securities Associates, Inc. ("CSA") are subject to certain requirements of the SEC with regard to liquidity and capital requirements. At June 30, 2006, SN & Co. had net capital of \$104.4 million, which was 32.00% of its aggregate debit items, and \$97.9 million in excess of the minimum required net capital and CSA had net capital of \$3.0 million, which was \$2.9 million in excess of minimum required net capital. SN & Co. and CSA may not be able to pay cash dividends from its equity capital without prior regulatory approval if doing so would jeopardize their ability to satisfy minimum net capital requirements.

The Company's international subsidiary, Stifel Nicolaus Limited, is subject to the regulatory supervision and requirements of the Financial Services Authority ("FSA") in the United Kingdom. The FSA also has the power to set minimum capital requirements, which Stifel Nicolaus Limited has met.

The Company receives a tax benefit for the conversion of stock based awards utilized to reduce the Company's income tax liability. The benefit is derived from the difference in the market value on the date the awards are converted and the share value on the date the awards were granted. For the first six months of 2006, the Company recorded \$10.2 million in income tax benefits.

Management believes the funds from operations, available informal short-term credit arrangements, and its ability to raise additional capital will provide sufficient resources to meet the present and anticipated financing needs.



## Recent Accounting Pronouncements

In March 2005, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations, an interpretation of Statement of Financial Accounting Standards ("SFAS") No. 143, Accounting for Asset Retirement Obligations ("FIN 47)". FIN 47 clarifies the term conditional asset retirement obligation as used in SFAS No. 143. FIN 47 refers to a legal obligation to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. Accordingly, an entity is required to recognize a liability for the fair value of a conditional asset retirement obligation if the fair value of the liability can be reasonably estimated. The Company's adoption of FIN 47 did not have a material impact on the Condensed Consolidated Financial Statements.

In June 2005, the Emerging Issues Task Force ("EITF") reached a consensus on EITF Issue No. 04-5, "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights" ("EITF No. 04-5"). EITF No. 04-5 consensus requires a general partner in a limited partnership to consolidate the limited partnership unless the presumption of control is overcome. The general partner may overcome this presumption of control and not consolidate the entity if the limited partners have: (a) the substantive ability to dissolve or liquidate the limited partnership or otherwise remove the general partner without having to show cause; or (b) substantive participating rights in managing the partnership. This consensus is effective for general partners of all new limited partnerships formed and for existing limited partnerships for which the partnership agreements are modified subsequent to the date of the ratification of this consensus (June 29, 2005). The adoption of EITF No. 04-5 did not have a material impact on the Company's Condensed Consolidated Financial Statements.

In June 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections - a replacement of APB Opinion No. 20 and FASB Statement No. 3," ("SFAS No. 154"). SFAS No. 154 changes the requirements for the accounting for and reporting of a change in accounting principle. The adoption of SFAS No. 154 did not have a material impact on the Company's Condensed Consolidated Financial Statements.

In June 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109* ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in a Company's financial statements and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 will be effective for the Company beginning in the first quarter of 2007. The Company is in the process of evaluating the impact of adopting FIN 48 on the Company's Condensed Consolidated Financial Statements.

## Contractual Obligations

The Company's contractual obligations are detailed in the Company's Annual Report on Form 10-K for the year-end December 31, 2005. As of June 30, 2006, the Company's contractual obligations have not materially changed from December 31, 2005.

## Item 3. Quantitative and Qualitative Disclosure about Market Risk

There have been no material changes from the information provided under "Item 7A. Quantitative and Qualitative Disclosures About Market Risk" in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

## Item 4. Controls and Procedures

As specified in the SEC's rules and forms, the Company's management, including Mr. Ronald J. Kruszewski as Chief Executive Officer and Mr. James M. Zemlyak as Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this quarterly report. Under rules promulgated by the SEC, disclosure controls and procedures are defined as those "controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms." Based on the evaluation of the Company's disclosure controls and procedures, the Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of June 30, 2006.

Further, as required by the SEC's rules and forms, the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the Company's internal control over financial reporting to determine whether any changes occurred during the quarter ended June 30, 2006 that have materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting. Based on that evaluation, there have been no such changes during the quarter ended June 30, 2006.

## PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company is named in and subject to various proceedings and claims incidental to its securities business activities, including lawsuits, arbitration claims and regulatory matters. While the ultimate outcome of pending litigation, claims and regulatory matters cannot be predicted with certainty, based upon information currently known, management believes that resolution of all such matters will not have a material adverse effect on the condensed consolidated financial condition of the Company but could be material to its operating results in one or more future periods. It is reasonably possible that certain of these lawsuits, arbitrations, claims and regulatory matters could be resolved in the next year and management does not believe such resolutions will result in losses materially in excess of the amounts previously provided.

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

## Issuer Purchases of Equity Securities

The following table summarizes the Company's repurchase activity of its common stock during the second quarter ended June 30, 2006:

| (Periods)                      | Total Number<br>of Shares<br>Purchased | Average<br>Price Paid<br>per Share | Total Number                                                           |                                                                                      |
|--------------------------------|----------------------------------------|------------------------------------|------------------------------------------------------------------------|--------------------------------------------------------------------------------------|
|                                |                                        |                                    | of Shares<br>Purchased<br>as Part of<br>Publicly<br>Announced<br>Plans | Maximum<br>Number of<br>Shares that<br>May Yet Be<br>Purchased<br>Under the<br>Plans |
| April 1, 2006 - April 30, 2006 | - -                                    | \$ - -                             | - -                                                                    | 2,078,977                                                                            |
| May 1, 2006 - May 31, 2006     | - -                                    | \$ - -                             | - -                                                                    | 2,078,977                                                                            |
| June 1, 2006 - June 30, 2006   | 73,500                                 | \$ 33.81                           | 73,500                                                                 | 2,005,477                                                                            |
| Total                          | 73,500                                 | \$ 33.81                           | 73,500                                                                 |                                                                                      |

The Company has an ongoing authorization, as amended, from the Board of Directors to repurchase its common stock in the open market or in negotiated transactions. In May 2005, the Company's Board of Directors authorized the repurchase of an additional 2,000,000 shares, for a total authorization to repurchase up to 3,000,000 shares.

Item 4. Submission of Matters to a Vote of Security Holders

The Annual Meeting of Stockholders of the Company was held on May 9, 2006. Of the 11,792,967 shares issued, outstanding and eligible to be voted at the meeting, 11,136,782 shares, constituting a quorum, were represented in person or by proxy at the meeting. Two matters were submitted to a vote of security holders at the meeting.

1. Election of Four Class II Directors. The first matter submitted was the election of four Class I director nominees to the Board of Directors, each to continue in office until the year 2009. Upon tabulation of the votes cast, it was determined that all four-director nominees had been elected. The voting results are set forth below:

| <u>Name</u>          | <u>For</u> | <u>Withheld</u> |
|----------------------|------------|-----------------|
| Charles A. Dill      | 10,801,740 | 335,042         |
| Richard F. Ford      | 10,823,233 | 313,549         |
| Richard J. Himelfarb | 10,850,486 | 286,296         |
| James M. Zemlyak     | 10,823,698 | 313,084         |

Because the Company has a staggered Board, the term of office of the following named Class I and III directors, who were not up for election at the 2006 annual meeting, continued after the meeting:

Class I

(to continue in office until 2008)

Robert J. Baer

Bruce A. Beda

Frederick O. Hanser

Ronald J. Kruszewski

Class III

(to continue in office until 2007)

John P. Dubinsky

Robert E. Lefton

Scott B. McCuaig

Thomas P. Mulroy

James M. Oates

Joseph A. Sullivan

2. Proposal to Ratify the Appointment of Deloitte & Touche LLP ("Deloitte").

The second matter, a proposal to ratify the appointment of Deloitte as the Company's independent registered public accounting firm for the year ending December 31, 2006, was approved by a majority of the 11,136,782 shares of the Company's common stock that were present and entitled to vote. The voting results on this matter were as follows:

|         |            |
|---------|------------|
| For     | 11,070,692 |
| Against | 64,483     |
| Abstain | 1,607      |

Item 6. Exhibits

(a) Exhibits

:

- 11 Statement re computation of per share earnings (set forth in "Note F - Stockholders Equity and Earnings Per Share ("EPS")" of the Notes to Condensed Consolidated Financial Statements (Unaudited))
- 31.1 Certification by the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification by the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. This exhibit is furnished to the SEC.

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SIGNATURES

Pursuant to the requirement 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.

STIFEL FINANCIAL CORP

·  
(Registrant)

Date: August 9, 2006

By: /s/ Ronald J. Kruszewski

Ronald J. Kruszewski  
(President and Chief Executive Officer)

Date: August 9, 2006

By: /s/ James M. Zemlyak

James M. Zemlyak  
(Principal Financial and Accounting Officer)

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EXHIBIT INDEX

| Exhibit No. | Description                                                                                                                                                             |
|-------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 31.1        | Certification by the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.                                                                 |
| 31.2        | Certification by the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.                                                                 |
| 32          | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.<br><i>This exhibit is furnished to the SEC.</i> |

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