BLACKSTONE MORTGAGE TRUST, INC.
Form 10-Q
May 06, 2013
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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 March 31, 2013

OR

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

For the transition period from _________ to _________

Commission File Number 1-14788

Blackstone Mortgage Trust, Inc.

(Exact name of registrant as specified in its charter)

Maryland	**94-6181186**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
345 Park Avenue, 10th Floor, New York, NY	**10154**
(Address of principal executive offices)	**(Zip Code)**

(212) 655-0220

(Registrant s telephone number, including area code)

Capital Trust, Inc.

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

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

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

The number of outstanding shares of the registrant s class A common stock, par value $0.01 per share, as of May 6, 2013 was 2,926,651 (after giving effect to the one-for-ten reverse stock split effected at 5:01 p.m. (EDT) on May 6, 2013).

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PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

Blackstone Mortgage Trust, Inc. and Subsidiaries

Consolidated Balance Sheets

March 31, 2013 and December 31, 2012

(in thousands, except per share data)

	March 31, 2013 (unaudited)	December 31, 2012
Assets		
Cash and cash equivalents	$ 15,361	$ 15,423
Restricted cash	12,719	14,246
Investment in CT Legacy Asset, at fair value		132,000
Securities, at fair value	11,702	
Loans receivable, at fair value	150,332	
Loans receivable, net	139,500	141,500
Loans held-for-sale, net	1,800	
Equity investments in unconsolidated subsidiaries	20,046	13,306
Accrued interest receivable, prepaid expenses, and other assets	13,693	5,868
Total assets	$ 365,153	$ 322,343
Liabilities & Equity		
Liabilities:		
Accounts payable, accrued expenses and other liabilities	$ 30,760	$ 21,209
Secured notes	8,671	8,497
Repurchase obligations	20,214	
Securitized debt obligations	136,944	139,184
Interest rate swap liabilities	6,119	
Total liabilities	202,708	168,890
Commitments and contingencies		
Equity:		
Class A common stock, $0.10 par value, 100,000 shares authorized, 2,927 shares issued and outstanding as of March 31, 2013 and December 31, 2012	293	293
Additional paid-in capital	609,040	609,002
Accumulated deficit	(533,238)	(535,851)
Total Blackstone Mortgage Trust, Inc. stockholders equity	76,095	73,444
Noncontrolling interests	86,350	80,009
Total equity	162,445	153,453

Total liabilities and equity	$ 365,153	$ 322,343

See accompanying notes to consolidated financial statements.

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Blackstone Mortgage Trust, Inc. and Subsidiaries

Consolidated Balance Sheets

March 31, 2013 and December 31, 2012

(in thousands, except per share data)

The following table presents the portion of the consolidated balances presented above attributable to consolidated variable interest entities, or VIEs. The following assets may only be used to settle obligations of these consolidated VIEs and these liabilities are only the obligations of these consolidated VIEs and they do not have recourse to the general credit of Blackstone Mortgage Trust, Inc.

	March 31, 2013 (unaudited)	December 31, 2012
Assets		
Loans receivable, net	$ 139,500	$ 141,500
Loans held-for-sale, net	1,800	
Accrued interest receivable, prepaid expenses, and other assets	2,433	4,021
Total assets	$ 143,733	$ 145,521
Liabilities		
Accounts payable, accrued expenses and other liabilities	$ 168	$ 88
Securitized debt obligations	136,944	139,184
Total liabilities	$ 137,112	$ 139,272

See accompanying notes to consolidated financial statements.

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Blackstone Mortgage Trust, Inc. and Subsidiaries

Consolidated Statements of Operations

Three Months Ended March 31, 2013 and 2012

(in thousands, except share and per share data)

(unaudited)

	Three Months Ended March 31, 2013	Three Months Ended March 31, 2012
Income from loans and other investments:		
Interest and related income	$ 1,456	$ 14,716
Less: Interest and related expenses	777	23,342
Income (loss) from loans and other investments, net	679	(8,626)
Other expenses:		
General and administrative	2,038	756
Total other expenses	2,038	756
Total other-than-temporary impairments of securities		
Portion of other-than-temporary impairments of securities recognized in other comprehensive income		(160)
Net impairments recognized in earnings		(160)
Recovery of provision for loan losses		8
Valuation allowance on loans held-for-sale	(200)	
Fair value adjustment on investment in CT Legacy Asset		3,954
Gain on deconsolidation of subsidiary		146,380
Income from equity investments		696
(Loss) income before income taxes	(1,559)	141,496
Income tax provision	38	301
(Loss) income from continuing operations	($ 1,597)	$ 141,195
Loss from discontinued operations, net of tax		(573)
Net (loss) income	($ 1,597)	$ 140,622
Net income attributable to noncontrolling interests	(1,518)	(74,069)
Net (loss) income attributable to Blackstone Mortgage Trust, Inc.	($ 3,115)	$ 66,553
Per share information:		
(Loss) income from continuing operations per share of common stock:		
Basic	($ 1.03)	$ 29.39

Diluted	($	1.03)	$	27.64
Loss from discontinued operations per share of common stock:				
Basic	$		($	0.25)
Diluted	$		($	0.25)
Net (loss) income per share of common stock:				
Basic	($	1.03)	$	29.14
Diluted	($	1.03)	$	27.39
Weighted average shares of common stock outstanding:				
Basic		3,016,425		2,283,741
Diluted		3,016,425		2,430,147

See accompanying notes to consolidated financial statements.

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Blackstone Mortgage Trust, Inc. and Subsidiaries

Consolidated Statements of Comprehensive (Loss) Income

For the Three Months Ended March 31, 2013 and 2012

(in thousands)

(unaudited)

	2013	2012
Net (loss) income	($ 1,597)	$ 140,622
Other comprehensive income:		
Unrealized gain on derivative financial instruments		2,267
Gain on interest rate swaps no longer designated as cash flow hedges		1,998
Amortization of unrealized gains and losses on securities		(756)
Amortization of deferred gains and losses on settlement of swaps		(56)
Other-than-temporary impairments of securities related to fair value adjustments in excess of expected credit losses, net of amortization		387
Other comprehensive income		3,840
Comprehensive (loss) income	($ 1,597)	$ 144,462
Less: Comprehensive income attributable to noncontrolling interests	(1,518)	(74,079)
Comprehensive (loss) income attributable to Blackstone Mortgage Trust, Inc.	($ 3,115)	$ 70,383

See accompanying notes to consolidated financial statements.

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Blackstone Mortgage Trust, Inc. and Subsidiaries

Consolidated Statements of Changes in (Deficit) Equity

For the Three Months Ended March 31, 2013 and 2012

(in thousands)

(unaudited)

	Class A Common Stock	Restricted Class A Common Stock	Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Accumulated Deficit	Total Blackstone Mortgage Trust, Inc. Stockholders (Deficit) Equity	Noncontrolling Interests	Total
Balance at January 1, 2012	$ 220	$ 2	$ 597,049	($ 40,584)	($ 667,111)	($ 110,424)	($ 18,515)	($ 128,939)
Net income					66,553	66,553	74,069	140,622
Other comprehensive income				3,830		3,830	10	3,840
Deconsolidation of CT Legacy Asset				1,293		1,293		1,293
Restricted class A common stock earned, net of shares deferred		1	125			126		126
Deferred directors compensation			56			56		56
Balance at March 31, 2012	$ 220	$ 3	$ 597,230	($ 35,461)	($ 600,558)	($ 38,566)	$ 55,564	$ 16,998
Balance at January 1, 2013	$ 293	$	$ 609,002	$	($ 535,851)	$ 73,444	$ 80,009	$ 153,453
Net loss					(3,115)	(3,115)	1,518	(1,597)
Consolidation of subsidiary					5,728	5,728	6,235	11,963
Distributions to noncontrolling interests							(1,412)	(1,412)
Deferred directors compensation			38			38		38
Balance at March 31, 2013	$ 293	$	$ 609,040	$	($ 533,238)	$ 76,095	$ 86,350	$ 162,445

See accompanying notes to consolidated financial statements.

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Blackstone Mortgage Trust, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

For the Three Months Ended March 31, 2013 and 2012

(in thousands)

(unaudited)

	2013	2012
Cash flows from operating activities:		
Net (loss) income	($ 1,597)	$ 140,622
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Net impairments recognized in earnings		160
Recovery of provision for loan losses		(8)
Valuation allowance on loans held-for-sale	200	
Fair value adjustment on CT Legacy Asset		(3,954)
Gain on deconsolidation of subsidiary		(146,380)
Income from equity investments in unconsolidated subsidiaries		(696)
Distributions of income from unconsolidated subsidiaries		61
Employee stock-based compensation		129
Incentive awards plan expense	963	(282)
Deferred directors compensation	38	56
Distributions from CT Legacy Asset		1,830
Amortization of premiums/discounts on loans and securities and deferred interest on loans		(171)
Amortization of deferred gains and losses on settlement of swaps		(56)
Amortization of deferred financing costs and premiums/discounts on debt obligations	174	8,813
Loss on interest rate swaps not designated as cash flow hedges		2,772
Changes in assets and liabilities, net:		
Accrued interest receivable	432	(2,999)
Deferred income taxes		(1,423)
Prepaid expenses and other assets	812	2,986
Accounts payable and accrued expenses	(266)	(182)
Net cash provided by operating activities	756	1,278
Cash flows from investing activities:		
Principal collections and proceeds from securities		21,496
Principal collections of loans receivable	1,135	83,000
Contributions to unconsolidated subsidiaries		(324)
Distributions from unconsolidated subsidiaries		677
Decrease in restricted cash	1,527	473
Net cash provided by investing activities	2,662	105,322
Cash flows from financing activities:		
Borrowings under repurchase obligations		123,977
Repayments under repurchase obligations		(58,464)
Repayments under mezzanine loan		(63,000)
Repayment of securitized debt obligations	(2,239)	(106,729)
Purchase of and distributions to noncontrolling interests	(1,097)	
Redemption of noncontrolling interests	(144)	

Vesting of restricted class A common stock		(4)
Net cash used in financing activities	(3,480)	(104,220)
Net (decrease) increase in cash and cash equivalents	($ 62)	$ 2,380
Cash and cash equivalents at beginning of period	15,423	34,818
Cash and cash equivalents at end of period	$ 15,361	$ 37,198

See accompanying notes to consolidated financial statements.

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Blackstone Mortgage Trust, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited)

Note 1. Organization

References herein to Blackstone Mortgage Trust, Company, we, us or our refer to Blackstone Mortgage Trust, Inc. and its subsidiaries unles context specifically requires otherwise.

We are a real estate finance company that focuses primarily on originating mortgage loans backed by commercial real estate assets. Our business plan is to originate, acquire and manage commercial real estate loans and securities and other commercial real estate-related debt instruments. Our investment objective is to preserve and protect our capital while producing attractive risk-adjusted returns primarily through dividends generated from current income on our portfolio.

From the inception of our finance business in 1997 through December 19, 2012, we were a fully integrated, self-managed, real estate finance and investment management company that invested for our own account directly on our balance sheet and for third parties through a series of investment management vehicles. On December 19, 2012, we consummated a strategic transaction that included, among other things, disposition of our investment management and special servicing business, including CT Investment Management Co., LLC, or CTIMCO, to an affiliate of The Blackstone Group L.P., or Blackstone. In conjunction with the sale, we entered into a management agreement with BREDS/CT Advisors L.L.C., which is an affiliate of Blackstone, whereby we became externally managed. We refer to BREDS/CT Advisors L.L.C. as our Manager, and we refer to the entire transaction as our Investment Management Business Sale.

We conduct our operations as a real estate investment trust, or REIT, for U.S. federal income tax purposes. We generally will not be subject to U.S. federal income taxes on our taxable income to the extent that we annually distribute all of our net taxable income to stockholders and maintain our qualification as a REIT. We also operate our business in a manner that permits us to maintain our exemption from registration under the Investment Company Act of 1940, as amended, or the Investment Company Act. We are organized as a holding company and conduct our business primarily through our various subsidiaries.

On April 26, 2013, our board of directors approved the change of our name from Capital Trust, Inc. to Blackstone Mortgage Trust, Inc., which we effected at 5:01 p.m. (EDT) on May 6, 2013 concurrently with a one-for-ten reverse stock split of our class A common stock. Except where the context indicates otherwise, all class A common stock numbers herein have been adjusted to give retroactive effect to the reverse stock split.

Sale of Investment Management Platform

On December 19, 2012, pursuant to a previously announced purchase and sale agreement, dated September 27, 2012, or Purchase Agreement, by and between us and Huskies Acquisition LLC, or Huskies Acquisition, an affiliate of Blackstone, and an assignment agreement, dated as of December 19, 2012 by and among us, Huskies Acquisition and Blackstone Holdings III L.P., or Holdings III, an affiliate of Blackstone, we completed the disposition of our investment management and special servicing business for a purchase price of $21.4 million. The sale included our equity interests in CTIMCO, our related private investment fund co-investments, and 100% of the outstanding class A preferred stock of CT Legacy REIT Mezz Borrower, Inc., or CT Legacy REIT. Pursuant to the terms of the Purchase Agreement, on December 19, 2012, we entered into a management agreement with our Manager, which was amended and restated as of March 26, 2013, pursuant to which we are now managed by our Manager pursuant to the terms and conditions of the management agreement. In addition, Blackstone received the right to designate two members of our board of directors, and exercised that right by designating an employee and one of its senior advisors to replace two former members of our board of directors who resigned effective December 19, 2012. As a result of the Investment Management Business Sale, the income and expense items related to our investment management business have been reclassified to income from discontinued operations on our consolidated statement of operations. See Note 8 for a further discussion of discontinued operations.

On December 19, 2012, we also closed our sale to Holdings III of 500,000 shares of our class A common stock for a purchase price of $10.0 million.

In connection with the consummation of the Investment Management Business Sale and the closing of our sale of 500,000 shares of class A common stock to Holdings III, we paid a previously announced $20.00 per share special cash dividend on December 20, 2012 to holders of record of our class A common stock at the close of business on November 12, 2012.

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Blackstone Mortgage Trust, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(unaudited)

The assets we retained following our Investment Management Business Sale consist primarily of: (i) our cash and cash equivalents of $15.4 million as of March 31, 2013, (ii) our interests in CT Legacy Partners, as defined below, a vehicle we formed to own and finance certain legacy assets that we retained in connection with a comprehensive debt restructuring in 2011, (iii) our carried interest in CT Opportunity Partners I, LP, or CTOPI, a private investment fund that was previously under our management and is now managed by an affiliate of our Manager, and (iv) our subordinated interests in certain collateral debt obligations, or CT CDOs.

CT CDO Deconsolidation

We have historically included the assets and liabilities of three CT CDOs in our consolidated balance sheet, CT CDO I, CT CDO II, and CT CDO IV. When we formed these CT CDOs, we retained residual debt and equity positions in each CT CDO, and CTIMCO serves as collateral manager of each CT CDO. As a result of the Investment Management Business Sale, we are no longer the collateral manager for our CT CDOs, nor the special servicer on their collateral assets. Due to the externalization of these management functions, and our lack of material economic interest in the residual equity we own in CT CDOs II and IV, we ceased to be the primary beneficiary of these entities and, therefore, discontinued the consolidation of CT CDOs II and IV as of December 19, 2012, which we refer to as the CT CDO Deconsolidation. We recognized a gain of $53.9 million on the deconsolidation of CT CDOs II and IV, which was due primarily to the reversal of charges to shareholders equity resulting from losses previously recorded in excess of our economic interests in these non-recourse securitization vehicles.

CT Legacy Partners Merger

To maintain its tax efficiency, on March 20, 2013, a majority of the stockholders of CT Legacy REIT voted in favor of a plan of merger, dated March 22, 2013, or the Merger, whereby CT Legacy REIT merged with and into CT Legacy Partners, LLC, or CT Legacy Partners, and whereby CT Legacy Partners was the surviving entity, effective as of March 22, 2013. As a result of the Merger, all outstanding shares of class A-1 common stock, class A-2 common stock, class B common stock, and class A preferred stock of CT Legacy REIT were converted into limited liability company shares, or LLC Shares, in CT Legacy Partners. These LLC Shares have economic and voting rights equivalent to the corresponding shares of stock of CT Legacy REIT. In addition, all outstanding shares of class B preferred stock of CT Legacy REIT were redeemed on March 21, 2013 for an aggregate $147,000, which amount is comprised of the shares par value, liquidation preference, and accrued dividends thereon.

As a result of the Merger, we have consolidated CT Legacy Partners as of March 20, 2013 and, therefore, the remaining legacy assets and liabilities from our comprehensive debt restructuring on March 31, 2011, which we refer to as our March 2011 Restructuring. See Note 3 for further discussion of CT Legacy Partners.

Structure of Notes to Consolidated Financial Statements

As of March 31, 2013, the majority of our asset and liabilities relate to either: (i) CT Legacy Partners, (ii) CTOPI, or (iii) CT CDO I. We have combined the disclosures of assets and liabilities related to each of these three portfolios to provide a better understanding of each portfolio s economic position and contribution to our consolidated balance sheet.

Note 2. Summary of Significant Accounting Policies

The accompanying unaudited consolidated interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States, or GAAP, 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 notes required by GAAP for complete financial statements. The accompanying unaudited consolidated interim financial statements should be read in conjunction with the consolidated financial statements and the related management s discussion and analysis of financial condition and results of operations filed with our Annual Report on Form 10-K for the fiscal year ended December 31, 2012. In our opinion, all material adjustments (consisting of normal, recurring accruals) considered necessary for a fair presentation, in accordance with GAAP, have been included. The results of operations for the three months ended March 31, 2013 are not necessarily indicative of results that may be expected for the entire year ending December 31, 2013.

Principles of Consolidation and Basis of Presentation

The accompanying financial statements include, on a consolidated basis, our accounts, the accounts of our wholly-owned subsidiaries, and variable interest entities, or VIEs, in which we are the primary beneficiary. All significant intercompany balances and transactions have been eliminated in consolidation.

Blackstone Mortgage Trust, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(unaudited)

VIEs are defined as entities in which equity investors (i) do not have the characteristics of a controlling financial interest, and/or (ii) do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. The entity that consolidates a VIE is known as its primary beneficiary, and is generally the entity with (i) the power to direct the activities that most significantly impact the VIE s economic performance, and (ii) the right to receive benefits from the VIE or the obligation to absorb losses of the VIE that could be significant to the VIE.

We have separately presented, following our consolidated balance sheet, the assets of consolidated VIEs that can only be used to satisfy the obligations of those VIEs, and the liabilities of consolidated VIEs that are non-recourse to us. We have aggregated all of such assets and liabilities of consolidated VIEs in this presentation due to our determination that these entities are substantively similar and therefore a further disaggregated presentation would not be more meaningful.

CT Legacy Partners accounts for its operations in accordance with industry-specific GAAP accounting guidance for investment companies, pursuant to which it reports its investments at fair value. We have retained this specialized accounting in consolidation and, accordingly, report the loans and securities investment of CT Legacy Partners at fair value on our consolidated balance sheet.

As more fully described in Note 1, we sold our investment management business to Blackstone in December 2012. As a result, the income and expense items related to our investment management business have been reclassified to income from discontinued operations on our consolidated statement of operations.

Certain reclassifications have been made in the presentation of the prior period consolidated financial statements to conform to the March 31, 2013 presentation.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may ultimately differ from those estimates.

Equity Investments in Unconsolidated Subsidiaries

Our carried interest in CTOPI is accounted for using the equity method. CTOPI s assets and liabilities are not consolidated into our financial statements due to our determination that (i) it is not a VIE and (ii) the investors have sufficient rights to preclude consolidation by us. As such, we report our allocable percentage of the net assets of CTOPI on our consolidated balance sheet. We have deferred the recognition of income from CTOPI until cash is collected or appropriate contingencies have been eliminated and, therefore do not recognize any income from equity investments in unconsolidated subsidiaries.

Revenue Recognition

Interest income from our loans receivable is recognized over the life of the investment using the effective interest method and is recorded on the accrual basis. Fees, premiums, discounts and direct costs associated with these investments are deferred until the loan is advanced and are then recognized over the term of the loan as an adjustment to yield. For loans where we have unfunded commitments, we amortize these fees and other items on a straight line basis. Fees on commitments that expire unused are recognized at expiration. Income accrual is generally suspended for loans at the earlier of the date at which payments become 90 days past due or when, in the opinion of our Manager, recovery of income and principal becomes doubtful. Income is then recorded on the basis of cash received until accrual is resumed when the loan becomes contractually current and performance is demonstrated to be resumed.

Interest income from our securities is recognized using a level yield with any purchase premium or discount accreted through income over the life of the security. This yield is calculated using cash flows expected to be collected which are based on a number of assumptions on the underlying loans. Examples include, among other things, the rate and timing of principal payments, including prepayments, repurchases, defaults and liquidations, the pass-through or coupon rate, and interest rates. Additional factors that may affect reported interest income on our securities include interest payment shortfalls due to delinquencies on the underlying mortgage loans and the timing and magnitude of expected credit losses on the mortgage loans underlying the securities. These are impacted by, among other things, the general condition of the real estate market, including competition for tenants and their related credit quality, and changes in market rental rates. These uncertainties and contingencies are difficult to predict and are subject to future events that may alter the assumptions.

Blackstone Mortgage Trust, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(unaudited)

Cash and Cash Equivalents

We classify highly liquid investments with original maturities of three months or less from the date of purchase as cash equivalents. We place our cash and cash equivalents with high credit quality institutions to minimize credit risk exposure. We may have bank balances in excess of federally insured amounts. We have not experienced, and do not expect, any losses on our demand deposits, commercial paper or money market investments.

Restricted Cash

We classify the cash balances held by CT Legacy Partners as restricted because, while these cash balances are available for use by CT Legacy Partners for operations, debt service, or other purposes, they cannot be used by us until our allocable share is distributed from CT Legacy Partners, and cannot be co-mingled with any of our other, unrestricted cash balances. See Note 3 for additional discussion of CT Legacy Partners.

Securities

We classify our securities as held-to-maturity, available-for-sale, or trading on the date of acquisition of the investment. Held-to-maturity investments are stated at cost, adjusted for the amortization of any premiums or discounts, which are amortized through our consolidated statements of operations using the level yield method described above. Other than in the instance of an other-than-temporary impairment, as discussed below, these held-to-maturity investments are carried on our consolidated financial statements at their amortized cost basis.

We may also invest in securities which may be classified as available-for-sale. Available-for-sale securities are carried at estimated fair value with the net unrealized gains or losses reported as a component of accumulated other comprehensive income (loss) in stockholders equity. Changes in the valuations do not affect our reported income or cash flows, but do impact stockholders equity and, accordingly, book value per share.

Further, as required under GAAP, when, based on current information and events, there has been an adverse change in the cash flows expected to be collected from those previously estimated for one of our securities, an other-than-temporary impairment is deemed to have occurred. A change in expected cash flows is considered adverse if the present value of the revised cash flows (taking into consideration both the timing and amount of cash flows expected to be collected) discounted using the security s current yield is less than the present value of the previously estimated remaining cash flows, adjusted for cash receipts during the intervening period.

Should an other-than-temporary impairment be deemed to have occurred, the security is written down to fair value. The total other-than-temporary impairment is bifurcated into (i) the amount related to expected credit losses, and (ii) the amount related to fair value adjustments in excess of expected credit losses, or the Valuation Adjustment. The portion of the other-than-temporary impairment related to expected credit losses is calculated by comparing the amortized cost basis of the security to the present value of cash flows expected to be collected, discounted at the security s current yield, and is recognized through earnings in the consolidated statement of operations. The remaining other-than-temporary impairment related to the Valuation Adjustment is recognized as a component of accumulated other comprehensive income (loss) in stockholders equity. A portion of other-than-temporary impairments recognized through earnings is accreted back to the amortized cost basis of the security through interest income, while amounts recognized through other comprehensive income (loss) are amortized over the life of the security with no impact on earnings.

Loans Receivable, Provision for Loan Losses, Loans Held-for-Sale and Related Allowance

We purchase and originate commercial real estate debt and related instruments generally to be held as long-term investments at amortized cost. We are required to periodically evaluate each of these loans for possible impairment. Impairment is indicated when it is deemed probable that we will not be able to collect all amounts due according to the contractual terms of the loan. If a loan is determined to be impaired, we write down the loan through a charge to the provision for loan losses. Impairment on these loans is measured by comparing the estimated fair value of the underlying collateral to the book value of the respective loan. These valuations require significant judgments, which include assumptions regarding capitalization rates, leasing, creditworthiness of major tenants, occupancy rates, availability of financing, exit plan, loan sponsorship, actions of other lenders and other factors deemed necessary by our Manager. Actual losses, if any, could ultimately differ from these estimates.

In conjunction with our quarterly loan portfolio review, our Manager assesses the performance of each loan, and assigns a risk rating based on several factors including risk of loss, loan-to-value ratio, or LTV, collateral performance, structure, exit plan, and sponsorship. Loans are rated one through eight, which ratings are defined as follows:

1 - **Low Risk:** A loan that is expected to perform through maturity, with relatively lower LTV, higher in-place debt yield, and stable projected cash flow.

Blackstone Mortgage Trust, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(unaudited)

2 - **Average Risk:** A loan that is expected to perform through maturity, with medium LTV, average in-place debt yield, and stable projected cash flow.

3 - **Acceptable Risk:** A loan that is expected to perform through maturity, with relatively higher LTV, acceptable in-place debt yield, and some uncertainty (due to lease rollover or other factors) in projected cash flow.

4 - **Higher Risk:** A loan that is expected to perform through maturity, but has exhibited a material deterioration in cash flow and/or other credit factors. If negative trends continue, default could occur.

5 - **Low Probability of Default/Loss:** A loan with one or more identified weakness that we expect to have a 15% probability of default or principal loss.

6 - **Medium Probability of Default/Loss:** A loan with one or more identified weakness that we expect to have a 33% probability of default or principal loss.

7 - **High Probability of Default/Loss:** A loan with one or more identified weakness that we expect to have a 67% or higher probability of default or principal loss.

8 - **In Default:** A loan which is in contractual default and/or which has a very high likelihood of principal loss.

In certain cases, we may classify loans as held-for-sale based upon the specific facts and circumstances of particular loans, including known or expected transactions. Loans held-for-sale are carried at the lower of their amortized cost basis and fair value. A reduction in the fair value of loans held-for-sale is recorded as a charge to our consolidated statement of operations as a valuation allowance on loans held-for-sale.

Deferred Financing Costs

The deferred financing costs which are included in prepaid expenses and other assets on our consolidated balance sheets include issuance costs related to our debt obligations, and are amortized using the effective interest method, or a method that approximates the effective interest method, over the life of the related obligations.

Repurchase Obligations

We record investments financed with repurchase obligations as a separate assets and the related borrowing under any repurchase agreement recorded as a liability on our consolidated balance sheets. Interest income earned on the investments and interest expense incurred on the repurchase obligations are reported separately on our consolidated statements of operations.

Interest Rate Derivative Financial Instruments

In the normal course of business, we use interest rate derivative financial instruments to manage, or hedge, cash flow variability caused by interest rate fluctuations. Specifically, we may use interest rate swaps to convert floating rate liabilities that are financing fixed rate assets into fixed rate liabilities. The differential to be paid or received on these agreements is recognized on the accrual basis as an adjustment to the interest expense related to the attendant liability. The interest rate swap agreements are generally accounted for on a held-to-maturity basis, and, in cases where they are terminated early, any gain or loss is generally amortized over the remaining life of the hedged item. These swap agreements must be effective in reducing the variability of cash flows of the hedged items in order to qualify for the aforementioned hedge accounting treatment. Changes in the fair value of effective cash flow hedges are reflected on our consolidated financial statements through accumulated other comprehensive income (loss) and do not affect our net income (loss). To the extent a derivative does not qualify for hedge accounting, and is deemed a non-hedge derivative, the changes in its fair value are included in net income (loss).

To determine the fair value of interest rate derivative financial instruments, we use a third-party derivative specialist to assist us in periodically valuing our interests.

Income Taxes

Our financial results generally do not reflect provisions for current or deferred income taxes on our REIT taxable income. We believe that we operate in a manner that will continue to allow us to be taxed as a REIT and, as a result, we generally do not expect to pay substantial corporate level taxes other than those payable by our taxable REIT subsidiaries. Many of these requirements, however, are highly technical and complex. If we were to fail to meet these requirements, we may be subject to federal, state and local income tax on current and past income, and penalties. See Note 9 for additional information.

Accounting for Stock-Based Compensation

Stock-based compensation expense is recognized in net income using a fair value measurement method, which we determine with the assistance of a third-party appraisal firm. Compensation expense for the time vesting of stock-based compensation grants is recognized on the accelerated attribution method and compensation expense for performance vesting of stock-based compensation grants is recognized on a straight line basis.

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The fair value of the performance vesting restricted class A common stock is measured on the grant date using a Monte Carlo simulation to estimate the probability of the market vesting conditions being satisfied. The Monte Carlo simulation is run approximately 100,000 times. For each simulation, the payoff is calculated at the settlement date, and is then discounted to the grant date at a risk-free interest rate. The average of the values over all simulations is the expected value of the restricted class A common stock on the grant date. The valuation is performed in a risk-neutral framework, so no assumption is made with respect to an equity risk premium. Significant assumptions used in the valuation include an expected term and stock price volatility, an estimated risk-free interest rate and an estimated dividend growth rate.

Comprehensive (Loss) Income

Total comprehensive (loss) income was ($1.6 million) and $144.5 million for the three months ended March 31, 2013 and 2012, respectively. The primary components of comprehensive income other than net income are the unrealized gains and losses on derivative financial instruments and the component of other-than-temporary impairments of securities related to the Valuation Adjustment.

Earnings per Share of Common Stock

Basic earnings per share, or EPS, is computed based on the net earnings allocable to common stock and stock units, divided by the weighted average number of shares of common stock and stock units outstanding during the period. Diluted EPS is determined using the treasury stock method, and is based on the net earnings allocable to common stock and stock units, divided by the weighted average number of shares of common stock, stock units and potentially dilutive common stock options and warrants. On April 26, 2013, our board of directors approved a one-for-ten reverse stock split of our class A common stock which we effected on May 6, 2013. Our earnings per share disclosures have been retroactively adjusted to reflect the reverse stock split.

We have separately determined EPS and diluted EPS for income (loss) from continuing operations and for net income (loss) allocable to common stockholders. See Note 6 for additional discussion of earnings per share.

Fair Value of Financial Instruments

The Fair Value Measurements and Disclosures Topic of the Financial Accounting Standards Board, or FASB, Accounting Standards Codification, or the Codification, defines fair value, establishes a framework for measuring fair value, and requires certain disclosures about fair value measurements under GAAP. Specifically, this guidance defines fair value based on exit price, or the price that would be received upon the sale of an asset or the transfer of a liability in an orderly transaction between market participants at the measurement date. Our assets and liabilities which are measured at fair value are discussed in Note 11.

Recent Accounting Pronouncements

In January 2013, the FASB issued Accounting Standards Update 2013-01, Balance Sheet (Topic 210): Clarifying the Scope of Disclosures About Offsetting Assets and Liabilities, or ASU 2013-01. ASU 2013-1 was developed to clarify which instruments and transactions are subject to the offsetting disclosure requirements set forth by Accounting Standards Update 2011-11 Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities. ASU 2013-01 is effective for the first interim or annual period beginning on or after January 1, 2013, and should be applied retrospectively for all comparative periods presented. The adoption of ASU 2013-1 did not have a material impact on our consolidated financial statements.

In February 2013, the FASB issued Accounting Standards Update 2013-02, Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income, or ASU 2013-02. ASU 2013-02 implements the previously deferred requirement to disclose reclassification adjustments into and out of accumulated other comprehensive income in either a note or on the face of the financial statements. ASU 2013-02 is effective for the first interim or annual period beginning after December 15, 2012, and should be applied prospectively. As we no longer have a balance of accumulated other comprehensive income as of December 31, 2012, we do not expect the adoption of ASU 2013-02 to have a material impact on our consolidated financial statements.

Note 3. CT Legacy Partners

As discussed in Note 1, CT Legacy Partners holds the remaining assets and liabilities of our legacy portfolio, which we had previously transferred to CT Legacy REIT (the predecessor of CT Legacy Partners) in connection with our March 2011 Restructuring. CT Legacy Partners is beneficially owned 52% by us and 48% by our former lenders. In

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addition, CT Legacy Partners has issued class B common shares, a subordinate class of equity which entitles its holders to receive approximately 25% of the dividends that would otherwise be payable to us on our equity interest in CT Legacy Partners, after aggregate cash distributions of $50.0 million have been paid to all other classes of common equity. Further, CT Legacy Partners has issued class A preferred shares which entitle its holder to cumulative preferred distributions in an amount generally equal to the greater of (i) 2.5% of certain of CT Legacy Partners assets, and (ii) $1.0 million per annum.

As of March 31, 2013, CT Legacy Partners had not made any distribution payments to its common equity holders.

Our equity interest in CT Legacy Partners is comprised of 4,393,750 class A-1 common shares, 775,000 class A-2 common shares, and 118,651 class B common shares. The outstanding common shares of CT Legacy Partners are comprised of 4.4 million class A-1 common shares, 5.6 million class A-2 common shares, and 1.5 million class B common shares. The equity interests of other members of CT Legacy Partners are reflected as noncontrolling interests on our consolidated balance sheet.

Net Investment in CT Legacy Partners

The following table details the components of our gross investment in CT Legacy Partners included in our consolidated balance sheet, as well as our net investment in CT Legacy Partners after the future payments under the secured notes and management incentive awards plan as of March 31, 2013 ($ in thousands):

Blackstone Mortgage Trust s Investment in CT Legacy Partners as of March 31, 2013

Gross investment in CT Legacy Partners:	
Restricted cash	$ 12,719
Securities, at fair value	11,702
Loans receivable, at fair value	150,332
Accrued interest receivable, prepaid expenses, and other assets	8,879
Accounts payable, accrued expenses and other liabilities	(815)
Repurchase obligations	(20,214)
Interest rate swap liabilities	(6,119)
Noncontrolling interests	(86,350)
	$ 70,134
Secured notes, including prepayment premium (1)	(11,059)
Management incentive awards plan, fully vested (2)	(10,563)
Net investment in CT Legacy Partners	$ 48,512

(1) Includes the full potential prepayment premium on secured notes, as described below. We carry this liability at its amortized basis of $8.7 million on our balance sheet as of March 31, 2013. The remaining interest and prepayment premium will be recognized, as applicable, over the term of the secured notes as a component of interest expense.

(2)

Assumes full payment of the management incentive awards plan, as described below, based on the hypothetical GAAP liquidation value of CT Legacy Partners as of March 31, 2013. We periodically accrue a payable for the management incentive awards plan based on the vesting schedule for the awards and continued employment with an affiliate of our Manager of the award recipients. As of March 31, 2013, our balance sheet includes $6.3 million in accounts payable and accrued expenses for the management incentive awards plan.

Secured Notes

In conjunction with our March 2011 Restructuring and the corresponding satisfaction of our senior credit facility and junior subordinated notes, certain wholly-owned subsidiaries of ours issued secured notes to these former creditors, which secured notes are non-recourse to us. The secured notes had an aggregate initial face value of $7.8 million and are secured by 93.5% of our equity interests in the class A-1 and class A-2 common shares of CT Legacy Partners, which represents 48.3% of the total outstanding class A-1 and class A-2 common shares of CT Legacy Partners. The secured notes mature on March 31, 2016 and bear interest at a rate of 8.2% per annum, which interest may be deferred until maturity. All distributions we receive from our equity interests in the common shares of CT Legacy Partners which serve as collateral under the secured notes must be used to pay, or prepay, interest and principal due thereunder, and only after the notes full satisfaction will we receive any cash flow from the common equity interests in CT Legacy Partners that serve as collateral for the notes. Any prepayment, or partial prepayment, of the secured notes will incur a prepayment premium resulting in a total payment of principal and interest under the secured notes of $11.1 million.

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We had secured notes outstanding with an accreted book value of $8.7 million and $8.5 million as of March 31, 2013 and December 31, 2012, respectively.

CT Legacy Partners Management Incentive Awards Plan

In conjunction with our March 2011 Restructuring, we created an employee pool for up to 6.75% of the distributions paid to the common equity holders of CT Legacy Partners (subject to certain caps and priority distributions). As of December 31, 2012, incentive awards for 92% of the pool were granted to our former employees, and the remainder remains unallocated. If any awards remain unallocated at the time distributions are paid, any amounts otherwise payable to the unallocated awards will be distributed pro-rata to the plan participants then employed by an affiliate of our Manager.

Approximately 82% of these grants have the following vesting schedule, which is contingent on continued employment with an affiliate of our Manager: (i) 25% vests on the date of grant, (ii) 25% vests in March 2013, (iii) 25% vests in March 2014, and (iv) the remainder vests upon our receipt of distributions from CT Legacy Partners. The remaining 18% of these grants vest upon our receipt of distributions from CT Legacy Partners.

We accrue a liability for the amounts due under these grants based on the value of CT Legacy Partners and the periodic vesting of the awards granted. Accrued payables for these awards were $6.3 million and $5.3 million as of March 31, 2013 and December 31, 2012, respectively.

A. Securities, at Fair Value CT Legacy Partners

CT Legacy Partners securities portfolio consists of CMBS and CDO securities. These securities had an aggregate principal balance of $135.3 million and are reported at their aggregate fair value of $11.7 million as of March 31, 2013. The following table details overall statistics for CT Legacy Partners securities portfolio as of March 31, 2013:

	March 31, 2013
Number of securities	12
Number of issues	6
Rating (1) (2)	CCC
Coupon (1) (3)	6.30%
Yield (1) (3)	5.67%
Life (years) (1) (4)	4.2

(1) Represents a weighted average as of March 31, 2013.
(2) Weighted average ratings are based on the lowest rating published by Fitch Ratings, Standard & Poor s or Moody s Investors Service for each security.
(3) Coupon is based on the securities contractual interest rates, while yield is based on expected cash flows for each security, and considers discounts/premiums and asset non-performance. Calculations for floating rate securities are based on LIBOR of 0.20% as of March 31, 2013.
(4) Weighted average life is based on the timing and amount of future expected principal payments through the expected repayment date of each respective investment.

We record CT Legacy Partners securities investments at fair value, which is determined using third party dealer assessments of value and our own internal financial model-based estimations. See Note 11 for further discussion of fair value.

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B. Loans Receivable, at Fair Value CT Legacy Partners

CT Legacy Partners loans receivable portfolio consisted of loans with an aggregate principal balance of $257.4 million, which are reported at their aggregate fair value of $150.3 million as of March 31, 2013. The following table details overall statistics for CT Legacy Partners loans receivable portfolio as of March 31, 2013 ($ in millions):

	March 31, 2013
Number of investments	12
Fixed / Floating [1]	$ 24 / $126
Coupon [2] [3]	6.48%
Yield [2] [3]	5.58%
Maturity (years) [2] [4]	1.2

(1) Represents the aggregate net book value of the portfolio allocated between fixed rate and floating rate loans
(2) Represents a weighted average as of March 31, 2013.
(3) Calculations for floating rate loans are based on LIBOR of 0.20% as of March 31, 2013.
(4) For loans in CT CDO I, assumes all extension options are executed. For loans in GSMS 2006-FL8A, maturity is based on information provided by its trustee.

We record CT Legacy Partners loans receivable investments at fair value, which is determined using our own internal financial model-based estimations. See Note 11 for further discussion of fair value.

The tables below detail the types of loans in CT Legacy Partners loan portfolio, as well as the property type and geographic distribution of the properties securing these loans, as of March 31, 2013 ($ in thousands):

	March 31, 2013	
Asset Type	**Book Value**	**Percentage**
Subordinate interests in mortgages	$ 80,853	54%
Mezzanine loans	43,265	29
Senior mortgages	26,214	17
Total	$ 150,332	100%

Property Type	Book Value	Percentage
Hotel	$ 50,653	34%
Office	43,844	29
Multifamily	12,814	9
Other	43,021	28
Total	$ 150,332	100%

Geographic Location	Book Value	Percentage
Northeast	$ 56,658	38%
Northwest	43,022	29
West	13,705	9
Southeast	11,931	8
International	25,016	16
Total	$ 150,332	100%

Loan risk ratings

Quarterly, our Manager evaluates CT Legacy Partners loan portfolio as described in Note 2. In conjunction with our quarterly loan portfolio review, our Manager assesses the performance of each loan, and assigns a risk rating based on several factors including risk of loss, LTV, collateral performance, structure, exit plan, and sponsorship. Loans are rated one (less risk) through eight (greater risk), which ratings are defined in Note 2.

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The following table allocates the net book value and principal balance of CT Legacy Partners loans receivable based on our internal risk ratings as of March 31, 2013 ($ in thousands):

	Loans Receivable as of March 31, 2013		
Risk Rating	**Number of Loans**	**Principal Balance**	**Net Book Value**
1 - 3	2	$ 32,683	$ 32,874
4 - 5	4	41,754	36,910
6 - 8	6	182,961	80,548
Total	12	$ 257,398	$ 150,332

In making this risk assessment, one of the primary factors we consider is how senior or junior each loan is relative to other debt obligations of the borrower. The following tables further allocate CT Legacy Partners loans receivable by both loan type and our internal risk ratings as of March 31, 2013 ($ in thousands):

	Senior Mortgage Loans as of March 31, 2013		
Risk Rating	**Number of Loans**	**Principal Balance**	**Net Book Value**
1 - 3		$	$
4 - 5	1	15,000	13,705
6 - 8	1	17,869	12,509
Total	2	$ 32,869	$ 26,214

	Subordinate Interests in Mortgages as of March 31, 2013		
Risk Rating	**Number of Loans**	**Principal Balance**	**Net Book Value**
1 - 3	1	$ 12,814	$ 12,814
4 - 5			
6 - 8	4	110,268	68,039
Total	5	$ 123,082	$ 80,853

	Mezzanine & Other Loans as of March 31, 2013		
Risk Rating	**Number of Loans**	**Principal Balance**	**Net Book Value**
1 - 3	1	$ 19,869	$ 20,060
4 - 5	3	26,754	23,205
6 - 8	1	54,824	
Total	5	$ 101,447	$ 43,265

Nonaccrual loans

In accordance with our revenue recognition policies discussed in Note 2, we do not accrue interest on loans which are 90 days past due or, in the opinion of our Manager, are otherwise uncollectable. Accordingly, we do not have any material interest receivable accrued on nonperforming loans as of March 31, 2013.

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The following table details CT Legacy Partners loans receivable which are on nonaccrual status as of March 31, 2013 ($ in thousands):

Non-Accrual Loans Receivable as of March 31, 2013

Asset Type	Principal Balance	Net Book Value
Senior Mortgage Loans	$	$
Subordinate Interests in Mortgages	43,448	
Mezzanine & Other Loans	69,146	11,931
Total	$ 112,594	$ 11,931

C. Repurchase Obligations CT Legacy Partners

As of March 31, 2013, CT Legacy Partners was party to a repurchase facility with JPMorgan with an outstanding balance of $20.2 million. The facility matures on December 15, 2014, and carries a rate of LIBOR+6.00% as of March 31, 2013.

The following table details the aggregate outstanding principal balance and fair value of CT Legacy Partners assets, primarily loans receivable, which were pledged as collateral under the JPMorgan repurchase facility as of March 31, 2013, as well as the amount at risk under the facility ($ in thousands). The amount at risk is generally equal to the book value of the collateral less the outstanding principal balance of the repurchase facility.

Repurchase Lender	Facility Balance	Loans and Securities Collateral Balances, Principal Balance	Loans and Securities Collateral Balances, Fair Value (1)	Amount at Risk (2)
JP Morgan	$ 20,214	$ 323,736	$ 162,034	$ 141,820

(1) Fair values represent the amount at which an asset could be sold in an orderly transaction between a willing buyer and willing seller. The immediate liquidation value of these assets would likely be substantially lower.

(2) Amount at risk is calculated on an asset-by-asset basis for the facility and considers the greater of (a) the book value of an asset and (b) the fair value of an asset, in determining the total risk.

D. Derivative Financial Instruments CT Legacy Partners

The following table summarizes the notional amounts and fair values of CT Legacy Partners interest rate swaps as of March 31, 2013 ($ in thousands). The notional amount provides an indication of the extent of CT Legacy Partners involvement in the instruments at that time, but it does not represent exposure to credit or interest rate risk.

Counterparty	March 31, 2013 Notional Amount	Interest Rate (1)	Maturity	March 31, 2013 Fair Value
JPMorgan Chase	$ 17,317	5.14%	2014	($ 990)

JPMorgan Chase		17,057	5.52%	2018	(2,672)
JPMorgan Chase		16,184	4.83%	2014	(1,146)
JPMorgan Chase		7,062	5.11%	2016	(921)
JPMorgan Chase		3,103	5.45%	2015	(390)
Total/Weighted Average	$	60,723	5.17%	2015	