Western Asset Mortgage Capital Corp
Form 10-K
March 16, 2015

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2014

OR

o **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: 001-35543

WESTERN ASSET MORTGAGE CAPITAL CORPORATION.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**27-0298092** (I.R.S. Employer Identification No.)

Western Asset Mortgage Capital Corporation
385 East Colorado Boulevard
Pasadena, California 91101
(Address of principal executive offices)

(626) 844-9400
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	**Name of Each Exchange on Which Registered**
Common Stock, $0.01 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No ý

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes o No ý

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 ý No o

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 ý No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ý

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 o	Accelerated filer ý	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

The aggregate market value of the registrant's common stock held by non-affiliates was $573,490,515 based on the closing sales price on the New York Stock Exchange on June 30, 2014.

On March 2, 2015, the registrant had a total of 41,719,801 shares of common stock outstanding.

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FORWARD-LOOKING INFORMATION

The Company makes forward-looking statements herein and will make forward-looking statements in future filings with the Securities and Exchange Commission (the "SEC"), press releases or other written or oral communications within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). For these statements, the Company claims the protections of the safe harbor for forward-looking statements contained in such sections. Forward-looking statements are subject to substantial risks and uncertainties, many of which are difficult to predict and are generally beyond the Company's control. These forward-looking statements include information about possible or assumed future results of the Company's business, financial condition, liquidity, results of operations, plans and objectives. When the Company uses the words "believe," "expect," "anticipate," "estimate," "plan," "continue," "intend," "should," "may" or similar expressions, the Company intends to identify forward-looking statements. Statements regarding the following subjects, among others, may be forward-looking: market trends in the Company's industry, interest rates, real estate values, the debt securities markets, the U.S. housing and the U.S. and foreign commercial real estate markets or the general economy or the demand for residential and/or commercial mortgage loans; the Company's business and investment strategy; the Company's projected operating results; actions and initiatives of the U.S. Government and changes to U.S. Government policies and the execution and impact of these actions, initiatives and policies; the state of the U.S. and to a lesser extent, international economy generally or in specific geographic regions; economic trends and economic recoveries; the Company's ability to obtain and maintain financing arrangements, including securitizations; the current potential return dynamics available in residential mortgage-backed securities ("RMBS"), and commercial mortgage-backed securities ("CMBS" and collectively with RMBS, "MBS"); the level of government involvement in the U.S. mortgage market; the anticipated default rates on Agency and Non-Agency MBS (as defined herein); the loss severity on Non-Agency MBS; the return of the Non-Agency RMBS, CMBS and asset-backed securities ("ABS") securitization markets; the general volatility of the securities markets in which the Company participates; changes in the value of the Company's assets; the Company's expected portfolio of assets; the Company's expected investment and underwriting process; interest rate mismatches between the Company's target assets and any borrowings used to fund such assets; changes in interest rates and the market value of the Company's target assets; changes in prepayment rates on the Company's target assets; effects of hedging instruments on the Company's target assets; rates of default or decreased recovery rates on the Company's target assets; the degree to which the Company's hedging strategies may or may not protect the Company from interest rate and foreign currency volatility; the impact of and changes in governmental regulations, tax law and rates, accounting guidance and similar matters; the Company's ability to maintain the Company's qualification as a real estate investment trust for U.S. federal income tax purposes; the Company's ability to maintain its exemption from registration under the Investment Company Act of 1940, as amended (the "1940 Act"); the availability of opportunities to acquire Agency RMBS, Non-Agency RMBS, CMBS, residential and/or commercial mortgage loans and other mortgage assets; the availability of opportunities to acquire ABS ; the availability of qualified personnel; estimates relating to the Company's ability to make distributions to its stockholders in the future; and the Company's understanding of its competition.

The forward-looking statements are based on the Company's beliefs, assumptions and expectations of its future performance, taking into account all information currently available to it. Forward-looking statements are not predictions of future events. These beliefs, assumptions and expectations can change as a result of many possible events or factors, not all of which are known to the Company. Some of these factors, are described in "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this annual report on Form 10-K. These and other risks, uncertainties and factors, including those described in the annual, quarterly and current reports that the Company files with the SEC, could cause its actual results to differ materially from those included in any forward-looking statements the Company makes. All forward-looking statements speak only as of the date they are made. New risks and uncertainties arise over time and it is not possible to predict those events or how they may affect the Company. Except as required by law, the Company is not obligated to, and does not intend to, update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

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Part I

Item 1. Business.

Overview

Western Asset Mortgage Capital Corporation and Subsidiaries (the "Company" unless otherwise indicated or except where the context otherwise requires "we", "us" or "our") upon commencing operations in May 2012, had an initial investment strategy which was primarily focused on investing in, financing and managing Agency RMBS (including TBAs as defined herein). Over time, we have expanded our investment strategy to include both Non-Agency RMBS and subsequently Agency and Non-Agency CMBS. In addition, and to a significantly lesser extent, we have invested in other securities including certain Agency obligations that are not technically MBS as well as certain Non U.S. CMBS and ABS investments secured by a portfolio private student loans and interests in residential whole-loans. These changes in our investment strategy, including future changes, are based on our Manager's perspective of which mix of portfolio assets it believes provides us with the best risk-reward opportunities at any given time. We have and expect to continue to finance our investment portfolio primarily through the use of repurchase agreements.

We operate and elected to be taxed as a real estate investment trust ("REIT"), commencing with our taxable year ended December 31, 2012. We generally will not be subject to U.S. federal income taxes on our taxable income to the extent that we annually distribute, in accordance with the REIT regulations, all of our net taxable income to stockholders and maintain our intended qualification as a REIT. We also intend to operate our business in a manner that will permit us to maintain our exemption from registration under the Act.

Our consolidated financial statements include our accounts, those of our wholly owned taxable REIT subsidiary or "TRS" and a trust that meets the definition of a variable interest entity ("VIE") related to the acquisition of residential whole-loans in which we are the primary beneficiary. The trust has issued trust certificates to us which are collateralized by pools of residential mortgage loans held by the trust. We include the underlying residential whole-loans owned by the trust in Residential whole-loans at fair value on our Consolidated Balance Sheets and have eliminated the trust certificates in consolidation.

We are externally managed and advised by Western Asset Management Company ("WAM", or the "Manager"), an SEC-registered investment advisor and a wholly-owned subsidiary of Legg Mason, Inc. Our Manager is responsible for administering our business activities and our day-to-day operations, subject to the supervision of our Board of Directors.

In light of the aforementioned developments and given our Manager's current market outlook and investment view, while we expect that Agency RMBS will continue to be a significant part of our portfolio, Agency RMBS will not necessarily be our primary investment in the future. Going forward, our Manager may vary the allocation among various asset classes subject to maintaining our qualification as a REIT under the federal tax law and maintaining our exemption from the 1940 Act. These restrictions limit our ability to invest in non-real estate assets and/or assets which are not secured by real estate. Accordingly, our portfolio will continue to be principally invested in MBS as well as other assets secured by real estate.

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On April 3, 2014, we entered into a binding agreement with a group of underwriters to sell an incremental 13.0 million shares of our common stock, which closed on April 9, 2014. The agreement provided the underwriters with the right to purchase an additional 1.95 million shares (15% of 13.0 million) during the succeeding thirty (30) days. The shares were offered to the market at a price of $14.85 per share and the underwriters exercised a portion of their option and purchased an incremental 1.0 million shares on May 2, 2014, which closed on May 7, 2014. We received net proceeds of approximately $205.4 million after subtracting underwriting commissions and offering expenses of approximately $2.9 million. On April 3, 2014, we also entered into an agreement to sell 650,000 shares of our common stock, for $14.85 per share, to our Manager in a private placement for an aggregate offering price of approximately $9.7 million, which closed on April 9, 2014.

We have invested the proceeds of our IPO, concurrent private placements and follow-on public offerings primarily in Agency RMBS, including Mortgage pass-through certificates, Agency derivatives, Agency Interest-Only Strips, and Agency CMOs; Non-Agency RMBS; Agency, Non-Agency and Non U.S. CMBS; ABS as well as residential whole-loans. We have also used "to-be-announced" forward contracts, or TBAs, in order to invest in Agency RMBS. Pursuant to these TBAs, we agree to purchase (or deliver), for future settlement, Agency RMBS with certain principal and interest terms. At December 31, 2014, our portfolio was comprised of approximately $3.2 billion of Agency RMBS (including approximately $257.6 million of Agency Interest-Only Strips), approximately $671.0 million of Non-Agency RMBS (including approximately $74.1 million of Non-Agency Interest-Only Strips), approximately $44.2 million of Agency CMBS (including approximately $18.8 million of Agency CMBS Interest-Only Strips), approximately $393.8 million of Non-Agency CMBS, approximately $108.9 million of other securities and approximately $7.2 million of residential whole-loans, exclusive of linked transactions. In addition, at December 31, 2014, our linked transactions included approximately $8.2 million of Non-Agency RMBS, approximately $38.6 million of Non-Agency CMBS (including Non U.S. CMBS) and approximately $5.7 million of other securities. To comply with the REIT requirements, some of our investments were held in a taxable REIT subsidiary or "TRS". By acquiring investments or engaging in activities through the TRS, it enables us to engage in such activities without endangering our REIT status. These investments or activities are not held or conducted at the REIT level and as a result would not impact our ability to maintain our qualification as a REIT.

We use leverage, currently consisting of borrowings under repurchase agreements, as part of our business strategy in order to increase potential returns to stockholders. We accomplish this by borrowing against existing MBS and other securities through repurchase agreements. There are no limits on the maximum amount of leverage that we may use, and we are not required to maintain any particular debt-to-equity leverage ratio under our charter. We may also change our financing strategy and leverage without the consent of stockholders.

As of December 31, 2014, we had entered into master repurchase agreements with 24 counterparties. As of December 31, 2014, we had approximately $3.9 billion of borrowings, including borrowings on linked transactions, outstanding under our repurchase agreements collateralized by approximately $4.4 billion of MBS and other securities. The balance outstanding at December 31, 2014 includes approximately $31.9 million related to linked transactions collateralized by approximately $52.5 million of MBS and other securities and $4.9 million of borrowings related to residential whole-loans owned through trust certificates of approximately $7.2 million. The trust certificates are eliminated upon consolidation. We have entered into swaps to effectively fix the interest rate of our borrowings; net of variable-rate payment swaps, of approximately $1.4 billion, under our repurchase agreements, and excluding forward starting swaps of $2.2 billion. In addition, as of December 31, 2014, we also owned swaptions on approximately an incremental $105.0 million of borrowings. As of December 31, 2014, our aggregate debt-to-equity ratio was approximately 6.3 to 1, including repurchase agreements on linked transactions and 6.2 to 1, excluding repurchase agreements on linked transactions.

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Our Investment Strategy

Our Manager's investment philosophy, which developed from a singular focus in fixed-income asset management over a variety of credit cycles and conditions, is to provide clients with diversified, tightly controlled, long-term value-oriented portfolios. Through rigorous analysis of all sectors of the fixed-income market, our Manager seeks to identify assets with the greatest risk-adjusted total value potential. In making investment decisions on our behalf, our Manager incorporates its views on the economic environment and the outlook for the mortgage markets, including relative valuation, supply and demand trends, the level of interest rates, the shape of the yield curve, prepayment rates, financing and liquidity, commercial and residential real estate prices, delinquencies, default rates, recovery of various segments of the economy and vintage of collateral, subject to maintaining our REIT qualification and our exemption from registration under the 1940 Act. We benefit from the breadth and depth of our Manager's overall investment philosophy, which focuses on a macroeconomic analysis as well as an in-depth analysis of individual assets and their relative value.

We rely on our Manager's expertise in asset allocation and identifying attractive assets within our investment strategy. At the time of our IPO, our core investment strategy was focused primarily on Agency RMBS. Our Manager's expertise in related investment disciplines such as Non-Agency RMBS, CMBS, and ABS has provided us with ability to include Non-Agency RMBS, Agency and Non-Agency CMBS, Non U.S. CMBS, ABS and other structured securities, as well as, providing valuable investment insights to our Agency RMBS investment selection and strategy.

We currently purchase and sell Agency RMBS (including TBAs) and Non-Agency RMBS, Agency and Non-Agency CMBS, Non U.S. CMBS, ABS as well as other structured securities, whole-loans and whole-loan securities. Currently, our Manager expects to expand our purchase of Non-Agency RMBS, Agency and Non-Agency CMBS, Non U.S. CMBS and ABS as well as expand our investment in whole-loans and whole-loan securities. We do not have specific investment guidelines providing for precise minimum or maximum allocations to any sector other than those necessary for maintaining our qualification as a REIT and our exemption from the 1940 Act. Our Manager has not and does not expect to purchase securities on our behalf with a view to selling them shortly after purchase. However, in order to maximize returns and manage portfolio risk while remaining opportunistic, we may dispose of securities earlier than anticipated or hold securities longer than anticipated depending upon prevailing market conditions, credit performance, availability of leverage or other factors regarding a particular security or our capital position.

Our Target Assets

We have invested the proceeds of our IPO, concurrent private placements and follow-on public offerings and expect to continue to focus on investing in the following types of securities:

Agency RMBS. Agency RMBS, which are RMBS for which the principal and interest payments are guaranteed by a U.S. Government agency, such as Government National Mortgage Association ("GNMA" or "Ginnie Mae"), or a U.S. Government-sponsored entity, such as Federal National Mortgage Association ("FNMA" or "Fannie Mae") or Federal Home Loan Mortgage Corporation ("FHLMC" or "Freddie Mac"). The Agency RMBS we acquire can be secured by fixed-rate mortgages, adjustable-rate mortgages or hybrid adjustable-rate mortgages. Fixed-rate mortgages have interest rates that are fixed for the term of the loan and do not adjust. The interest rates on adjustable-rate mortgages generally adjust annually (although some may adjust more frequently) to an increment over a specified interest rate index. Hybrid adjustable-rate mortgages have interest rates that are fixed for a specified period of time (typically three, five, seven or ten years) and, thereafter, adjust to an increment over a specified interest rate index. Adjustable-rate mortgages and hybrid adjustable-rate mortgages generally have periodic and lifetime constraints on the amount by which the loan interest rate can change on any predetermined interest rate reset date. As of December 31, 2014, all of our Agency RMBS, excluding interest-only strips, are secured by fixed-rate mortgages.

Mortgage pass-through certificates. Mortgage pass-through certificates are securities representing interests in "pools" of mortgage loans secured by residential real property where payments of both interest and scheduled principal, plus pre-paid principal, on the underlying loan pools are made monthly to holders of the securities, in effect "passing through" monthly payments made by the individual borrowers on the mortgage loans that underlie the securities, net of fees paid to the issuer/guarantor of the securities and servicers of the underlying mortgages.

Interest-Only Strips or IOs. This type of security only entitles the holder to interest payments. The yield to maturity of Interest-Only Strips is extremely sensitive to the rate of principal payments (particularly prepayments) on the underlying pool of mortgages. We invest in these types of securities primarily to take advantage of particularly attractive prepayment-related or structural opportunities in the MBS markets, as well as to help manage the duration of our overall portfolio

Inverse Interest-Only Strips or IIOs. This type of security has a coupon with an inverse relationship to its index and is subject to caps and floors. Inverse Interest-Only MBS entitles the holder to interest only payments based on a notional principal balance, which is typically equal to a fixed rate of interest on the notional principal balance less a floating rate of interest on the notional principal balance that adjusts according to an index subject to set minimum and maximum rates. The current yield of Inverse Interest-Only MBS will generally decrease when its related index rate increases and increase when its related index rate decreases.

Principal-Only Strips. This type of security generally only entitles the holder to receive cash flows that are derived from principal repayments of an underlying loan pool, but in the case of Non-Agency Principal-Only Strips will also include cash flows from default recoveries and excess interest. The yield to maturity of Principal-Only Strips is extremely sensitive to the rate of principal payments (particularly prepayments) on the underlying pool of mortgages. We invest in these types of securities primarily to take advantage of structural opportunities in the MBS markets.

TBAs. We may utilize TBAs, in order to invest in Agency RMBS. Pursuant to these TBAs, we agree to purchase (or deliver), for future settlement, Agency RMBS with certain principal and interest terms and certain types of underlying collateral, but the particular Agency RMBS to be delivered is not identified until shortly before the TBA settlement date. Our ability to invest in Agency RMBS through TBAs may be limited by the 75% income and asset tests applicable to REITs.

Collateralized Mortgage Obligations or CMOs. These are securities that are structured from residential and/or commercial pass-through certificates, which receive monthly payments of principal and interest. CMOs divide the cash flows which come from the underlying mortgage pass-through certificates into different classes of securities that may have different maturities and different weighted average lives than the underlying pass-through certificates.

Non-Agency RMBS. RMBS that are not guaranteed by a U.S. Government agency or U.S. Government-sponsored entity, with an emphasis on securities that when originally issued were rated in the highest rating category by one or more of the nationally recognized statistical rating organizations.

The mortgage loan collateral for Non-Agency RMBS consists of residential mortgage loans that do not generally conform to underwriting guidelines issued by a U.S. Government agency or U.S. Government-sponsored entity due to certain factors, including mortgage balances in excess of agency underwriting guidelines, borrower characteristics, loan characteristics and/or level of documentation, and therefore are not issued or guaranteed by a U.S. Government agency or U.S. Government-sponsored entity. The mortgage loan collateral may be classified as subprime, Alternative-A or prime depending on the borrower's credit rating and the underlying level of documentation. Non-Agency RMBS may be secured by fixed-rate mortgages, adjustable-rate mortgages or hybrid adjustable-rate mortgages.

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Agency CMBS. Fixed and floating rate CMBS, for which the principal and interest payments are guaranteed by a U.S. Government agency or U.S. Government-sponsored entity, but for which the underlying mortgage loans are secured by real property other than single family residences. These may include, but are not limited to Fannie Mae DUS (Delegated Underwriting and Servicing) MBS, Freddie Mac Multifamily Mortgage Participation Certificates, Ginnie Mae project loan pools, and/or CMOs structured from such collateral.

Non-Agency CMBS. Fixed and floating rate CMBS for which the principal and interest payments are not guaranteed by a U.S. Government agency or U.S. Government-sponsored entity. To date, our primary emphasis has been on legacy securities that when originally issued were rated in the highest rating category by one or more of the nationally recognized statistical rating organizations but we have also invested in subordinated debt for which the property (properties) securing the underlying mortgage collateral is located within the U. S. or the European Union. We do not have an established a minimum current rating requirement for such investments.

Non U.S. CMBS. CMBS which is not guaranteed by a U.S. Government agency or U.S. Government-sponsored entity and which is secured by commercial real estate located outside of the U.S. Although our Manager believes that these investments can provide attractive risk-reward opportunities and offer additional asset diversification, investing in international real estate has a number of additional risks, including but not limited to currency risk, political risk and the legal risk of investing in jurisdiction(s) with varying laws and regulations and potential tax implications. See Item 7A: Quantitative and Qualitative Disclosures about Market Risk Foreign Investment Risk and Currency Risk herein.

Agency and Non-Agency CMBS IO and IIO Securities. Interest-Only and Inverse Interest-Only securities for which the underlying collateral is commercial mortgages the principal and interest on which may or may not be guaranteed by a U.S Government agency or U.S. Government-sponsored entity. Unlike single family residential mortgages in which the borrower, generally, can prepay at any time, commercial mortgages frequently limit the ability of the borrower to prepay, thereby providing a certain level of prepayment protection. Common restrictions include yield maintenance and prepayment penalties, the proceeds of which are generally at least partially allocable to these securities, as well as defeasance.

Risk Sharing Securities Issued by Fannie Mae and Freddie Mac. From time to time we have and may in the future continue to invest in risk sharing securities issued by Fannie Mae and Freddie Mac. Principal and interest payments on these securities are based on the performance of a specified pool of Agency residential mortgages. The payments due on these securities, however, are not secured by the referenced mortgages, but are full faith and credit obligations of Fannie Mae or Freddie Mac respectively. Investments in these securities generally are not qualifying assets for purposes of the 75% asset test applicable to REITs and generally do not generate qualifying income for purposes of the 75% income test applicable to REITs. As a result, we may be limited in our ability to invest in such assets.

ABS. Debt and/or equity tranches of securitizations backed by various asset classes including, but not limited to, aircrafts, automobiles, credit cards, equipment, franchises, recreational vehicles and student loans. Investments in ABS generally are not qualifying assets for purposes of the 75% asset test applicable to REITs and generally do not generate qualifying income for purposes of the 75% income test applicable to REITs. As a result, we may be limited in our ability to invest in such assets.

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Residential whole-loans. We have made our first investment in "residential whole-loan" instruments and may in the future expand our investment in these mortgages, secured by single family residential properties. In this regard, our Manager is actively working on a number of potential whole-loan programs involving residential mortgages. As currently contemplated, these programs involve investing in structured Non-Agency RMBS programs crafted specifically for us, although it is possible that we could hold mortgage loans directly at some point. In addition to holding these instruments for investment, our Manager is also working to provide us with the ability to invest in or acquire whole-loans directly or gain exposure to whole-loans through investments in structured programs with the intention of securitizing the whole-loans in the future, selling the investment grade portion of the securitized structure and retaining the residual portion. During the fourth quarter 2014, we completed our first purchase of these instruments. The residential whole-loans are held by a trust whose entire beneficial interest we hold. Although our expectation is that we will continue to make at least a limited amount of these investments in the near future, increasing these instruments as part of our target assets involves complex investment, structural, regulatory and accounting issues and there can be no assurance that we will in fact expand our investments in residential whole-loans or, if we do, in what form and to what extent we will do so.

Commercial whole-loans. Our Manager is also actively exploring opportunities to invest in small balance, $2.5 million to $25.0 million, commercial whole-loans, including commercial mortgages and Small Business Administration or SBA loans secured primarily by real estate. Subsequent to the close of the fiscal year, we made our first investment in these instruments. While our Manager has experience in CMBS and we currently invest in Agency and Non-Agency CMBS as well as Non U.S. CMBS, investing in whole-loans backed or secured by commercial real estate assets involves complex investment, structural, regulatory and accounting issues. Some of these issues are unique to commercial whole-loans as opposed to residential mortgages. Accordingly, there is no assurance of the prevalence such investments will have in our overall portfolio.

Other investments. In addition to MBS, our principal investment, and ABS from time to time, we may also make other investments in securities, which our Manager believes will assist us in meeting our investment objective and are consistent with our overall investment policies. These investments will normally be limited by the REIT requirements that 75% our assets be real estate assets and that 75% of our income be generated from real estate, thereby limiting our ability to invest in such assets.

At the time of our IPO, our primary investment strategy focused on Agency RMBS. As discussed above, we continue to increase the portion of our portfolio allocated to Non-Agency RMBS, Agency and Non-Agency CMBS, Non U.S. CMBS and ABS and in the fourth quarter of 2014 made our first in investment in residential whole-loan mortgages. In the future are likely to expand our investments in these securities. The allocation to Non-Agency RMBS, Agency and Non-Agency CMBS, residential and commercial whole-loans and ABS may vary from time to time based on market conditions.

As of December 31, 2014, the fair value of our investment portfolio was comprised of 72.0% of Agency RMBS, 15.3% of Non-Agency RMBS, 1.0% of Agency CMBS, 9.0% of Non-Agency CMBS, 2.5% of other securities and 0.2% of residential whole-loans, excluding linked transactions. As of December 31, 2014, the fair value of our investment portfolio was comprised of 71.2% of Agency RMBS, 15.3% of Non-Agency RMBS, 1.0% of Agency CMBS, 9.7% of Non-Agency CMBS, 2.6% of other securities and 0.2% of residential whole-loans, including linked transactions.

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Our Financing Strategy.

The leverage that we employ is specific to each asset class and is determined based on several factors, including potential asset price volatility, margin requirements, the current cycle for interest rates, the shape of the yield curve, the outlook for interest rates and our ability to use and the effectiveness of interest rate hedges. We analyze both historical volatility and market-driven implied volatility for each asset class in order to determine potential asset price volatility. Our leverage targets attempt to risk-adjust asset classes based on each asset class's potential price volatility. The goal of our leverage strategy is to ensure that, at all times, our investment portfolio's overall leverage ratio is appropriate for the level of risk inherent in the investment portfolio.

We may fund the acquisition of our assets through the use of leverage from a number of financing sources, subject to maintaining our qualification as a REIT. We finance purchases of MBS and other securities primarily through the use of repurchase agreements.

Our operating results depend in large part on differences between the income earned on our assets and our cost of borrowing and hedging activities. We use leverage to increase potential returns to our stockholders. We currently accomplish this by borrowing against existing assets through repurchase agreements. Our investment policies place no limits on the maximum amount of leverage that we may use, and we are not required to maintain any particular debt-to-equity leverage ratio under our charter. We may also change our financing strategy and leverage without the consent of our stockholders.

The costs associated with our borrowings are generally based on prevailing market interest rates. During a period of rising interest rates, our borrowing costs generally will increase while the yields earned on our existing portfolio of leveraged fixed-rate MBS and other fixed rate securities will remain static. This could result in a decline in our net interest spread and net interest margin. The severity of any such decline would depend on our asset/liability composition at the time, as well as the magnitude and duration of the interest rate increase. Further, an increase in short-term interest rates could also have a negative impact on the market value of our assets. If either of these events happens, we could experience a decrease in net income or incur a net loss during these periods, which could adversely affect our liquidity and results of operations.

We expect to maintain a debt to equity ratio of five to ten times the amount of our stockholders' equity, although there is no minimum or maximum leverage that our investment policies explicitly require. To the extent the Agency MBS percentage of our portfolio decreases, our overall leverage is likely to decrease. Depending on the different cost of borrowing funds at different maturities, we will vary the maturities of our borrowed funds to attempt to produce lower borrowing costs and reduce interest rate risk. We enter into collateralized borrowings only with institutions that are rated investment grade by at least one nationally-recognized statistical rating organization. We rely on financing to acquire, on a leveraged basis, assets in which we invest. If market conditions deteriorate, our lenders may exit the repurchase market, and tighten lending standards, or increase the amount of equity capital required to obtain financing making it more difficult and costly for us to obtain financing.

For the year ended December 31, 2014, we financed our MBS and other securities with repurchase agreements, on a debt-to-equity basis, ranging from 6.1 to 7.4 times leverage calculated at each month-end. In the future, we may, however, be limited or restricted in the amount of leverage we may employ by the terms and provisions of any financing or other agreements, and may be subject to margin calls as a result of our financing activity. We had an aggregate debt-to-equity ratio, related to our repurchase agreements of approximately 6.3 to 1, including repurchase agreements on linked transactions, and 6.2 to 1, excluding repurchase agreements on linked transactions at December 31, 2014. Our debt-to-equity ratio is computed by dividing repurchase borrowings by total stockholders' equity.

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We finance MBS and other securities with repurchase agreement financing with maturities generally ranging from one to three months, but in some cases longer. At December 31, 2014, we had entered into master repurchase agreements with 24 counterparties. One of our existing repurchase agreement counterparties and one of its affiliates has communicated their intention to exit the repurchase agreement market in 2015. We believe that we have sufficient capacity with our other repurchase agreement counterparties to refinance these positions. We had approximately $3.9 billion outstanding under our repurchase agreements, including repurchase agreements accounted for as part of linked transactions of $28.9 million and repurchase agreements related to residential whole-loans owned through trust certificates of $4.9 million at December 31, 2014. The trust certificates are eliminated upon consolidation.

Our Hedging Strategy

Subject to maintaining our qualification as a REIT for U.S. federal income purposes, we pursue various economic hedging strategies to seek to reduce our exposure to adverse changes in interest rates and, to a more limited extent, foreign currency. The U.S. federal income tax rules applicable to REITs may require us to implement certain of these techniques through a domestic TRS that is fully subject to federal corporate income taxation. As of December 31, 2014, we have one wholly owned subsidiary which we have jointly elected to treat as a TRS. Our hedging activity varies in scope based on the level and volatility of interest rates, the type of assets held, including currency denomination and other changing market conditions. As of December 31, 2014, the majority of swaps we entered into are designed to mitigate the effects of increases in interest rates under a portion of our repurchase agreements. These swaps generally provide for fixed interest rates indexed off of the London interbank offered rate or LIBOR and effectively fix the floating interest rates. Notwithstanding the foregoing, in order to manage our hedge position with regard to our liabilities, we on occasion will enter into interest rate swaps which involve the receipt of fixed-rate amounts from a counterparty in exchange for us making variable-rate payments over the life of the interest rate swap without exchange of the underlying notional amount. As of December 31, 2014, we effectively fixed the floating interest rates on approximately $1.4 billion of borrowings under our repurchase agreements, net of variable-rate payment swaps. We also entered into forward starting swaps of $2.2 billion. We utilize forward starting swaps and swaptions for several reasons including replacing expiring swaps, in anticipation of increasing our overall financing and reducing our exposure to future interest rate increases. Interest rate swaptions provide us the option to enter into an interest rate swap agreement for a predetermined notional amount, stated term and pay and receive interest rates in the future. As of December 31, 2014, we owned swaptions on approximately an incremental $105.0 million of borrowings. As of December 31, 2014, we also entered into foreign currency swaps, agreeing to pay a fixed amount of euros in exchange for a fixed amount of U.S. dollars as well as currency forwards. We entered into the currency swaps and forwards in order to hedge our exposure to foreign currency with respect to Non-U.S. CMBS investments and the corresponding repurchase financings utilized to make such investments. In order to enable us to maintain compliance with the REIT requirements, we have generally elected to treat our derivative instruments as hedges for U.S. federal tax purposes. To date, however, we have not elected to apply hedge accounting for financial statement reporting purposes for our derivative instruments. As a result, we record the change in fair value of our derivatives and the associated interest and currency exchange in earnings. Additionally, we may enter into hedging transactions in the form of puts and calls or other financial instruments that we deem appropriate.

Our interest rate hedging techniques are partly based on assumed levels of prepayments of our target assets. If prepayments are slower or faster than assumed, the life of the investment will be longer or shorter, which would reduce the effectiveness of any of the interest rate hedging strategies we may use and may cause losses on such transactions. Hedging strategies, both interest rate and foreign currency, involve the use of derivative securities which are highly complex and may produce volatile returns.

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We may invest in equity index derivatives such as futures, options on futures and options on indices. These instruments are used normally to hedge interest rate movements as well as credit risks and other risks associated with our portfolio which may be impacted by volatility in the equity markets. Tax and other regulatory rules may limit our overall ability to use these instruments even through a TRS. Investing in these instruments introduces equity market risks into the management of the portfolio although as noted above our Manager uses them for the purpose of hedging our overall interest rate risk. These hedging strategies involving equity index products may not be successful, and may expose us to additional losses, if expected correlations between such risks and the equity markets do not occur. The goal of our hedging strategy is to ensure that, at all times, we are appropriately hedged in accordance with the REIT requirements for the level of interest rate and currency risk inherent in our investment portfolio.

Regulation

Our Manager

We are externally managed and advised by Western Asset Management Company. Established in 1971 and acquired by Legg Mason in 1986, our Manager is a registered investment advisor headquartered in Pasadena, California, that specializes in fixed-income asset management. From offices in Pasadena, Dubai, Hong Kong, London, Melbourne, New York, São Paulo, Singapore and Tokyo, our Manager's 824 employees provide investment services for a wide variety of global clients, including mutual funds, corporate, public, insurance, health care, union organizations and charitable foundations. As of December 31, 2014, our Manager and its investment advisory affiliates over which our Manager has operational responsibility, or its supervised affiliates, had approximately $466.0 billion in assets under management. All of our officers, apart from our chief financial officer, Steven M. Sherwyn, were employees of our Manager previous to January 1, 2014. Effective on that date, Mr. Sherwyn also became an employee of our Manager as well. In addition two, of our directors, James W. Hirschmann III and Gavin L. James, are also employees of our Manager. Our Manager is responsible for, among other duties: (i) performing all of our day-to-day functions; (ii) determining investment criteria in conjunction with our Board of Directors; (iii) sourcing, analyzing and executing investments, asset sales and financings; (iv) performing asset management duties; and (v) performing financial and accounting management.

Management Agreement

On May 9, 2012, we entered into a management agreement, or the Management Agreement, with our Manager. Pursuant to the Management Agreement, our Manager is responsible for the implementation of our business strategy and performs certain services for us, subject to oversight by our Board of Directors. The initial term of the Management Agreement ends on May 15, 2015, with automatic one-year renewal terms thereafter. Following the initial three-year term, the Management Agreement may be terminated annually upon the affirmative vote of at least two thirds ($^2/_3$) of our independent directors based upon: (i) our Manager's unsatisfactory performance that is materially detrimental to us; or (ii) our determination that any fees payable to our Manager are not fair, subject to our Manager's right to prevent termination based on unfair fees by accepting a reduction of management fees agreed to by at least two thirds ($^2/_3$) of our independent directors, subject to 180 days prior notice of such termination. Upon such a termination, we are required to pay our Manager a termination fee equal to three times the average annual management fee earned by our Manager during the prior 24-month period prior to such termination. We may also terminate the Management Agreement at any time, including during the initial term, with 30 days prior notice from our Board of Directors, without payment of a termination fee, for cause, as defined in the Management Agreement. Our Manager may terminate the Management Agreement if we become required to register as an investment company under the 1940 Act, with such termination deemed to occur immediately before such event, in which case we are not required to pay a termination fee. Our Manager may also decline to renew the Management Agreement by providing us with 180 days written notice, in which case we are not required to pay a termination fee. Pursuant to the terms of the Management Agreement it has been extended for one year to May 15, 2016.

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Our Manager is entitled to a management fee equal to 1.5% per annum, calculated and payable quarterly in arrears, of our stockholders' equity. For purposes of calculating the management fee, our "stockholders' equity" means the sum of the net proceeds from any issuances of our equity securities since inception (allocated on a pro rata daily basis for such issuances during the fiscal quarter of any such issuance), plus our retained earnings, calculated in accordance with U.S. GAAP, at the end of the most recently completed fiscal quarter (without taking into account any non-cash equity compensation expense incurred in current or prior periods), less any amount that we pay for repurchases of our shares of common stock, excluding any unrealized gains, losses or other non-cash items that have impacted stockholders' equity as reported in our financial statements prepared in accordance with U.S. GAAP, regardless of whether such items are included in other comprehensive income or loss, or in net income, including OTTI charges reported in other loss on MBS, unrealized gain (loss) on MBS and other securities and the non-cash portion of gain (loss) on derivative instruments, as well as one-time events pursuant to changes in U.S. GAAP and certain other non-cash charges, based on discussions between our Manager and our independent directors and subject to approval by at least two thirds (2/3) of our independent directors. However, if our stockholders' equity for any given quarter is negative based on the calculation described above, our Manager will not be entitled to receive any management fee for that quarter. Our Manager is entitled to reimbursement of its operating expenses related to us, including legal, accounting, due diligence and other services.

We elected to be taxed as a REIT under Section 856 through 860 of the Internal Revenue Code of 1986, as amended (the "Code"), commencing with our taxable year ended December 31, 2012. We will generally not be subject to corporate U.S. federal or state income tax to the extent that we make qualifying distributions to stockholders, and provided that we satisfy, on a continuing basis, through actual investment and operating results, the REIT requirements including certain asset, income, distribution and stock ownership tests. If we fail to qualify as a REIT, and do not qualify for certain statutory relief provisions, we will be subject to U.S. federal, state and local income taxes and may be precluded from qualifying as a REIT for the subsequent four taxable years following the year in which we lost our REIT qualification. The failure to qualify as a REIT could have a material adverse impact on the Company's results of operations and amounts available for distribution to stockholders.

We believe that we are not, and intend to conduct our operations so as not to become regulated as an investment company under the 1940 Act. We have relied, and intend to continue to rely on current interpretations of the staff of the SEC in an effort to continue to qualify for an exemption from registration under the 1940 Act. For more information on the exemptions that we utilize refer to Item 1A, "Risk Factors" of this annual report on Form 10-K.

Competition

Our net income depends, in part, on our ability to acquire assets at favorable spreads over our borrowing costs. In acquiring our target assets, we compete with other REITs, specialty finance companies, savings and loan associations, banks, mortgage bankers, insurance companies, mutual funds, institutional investors, investment banking firms, financial institutions, governmental bodies and other entities. In addition, other REITs with similar asset acquisition objectives, including a number that have been recently formed and others that may be organized in the future, compete with us in acquiring assets and obtaining financing. These competitors may be significantly larger than us, may have access to greater capital and other resources or may have other advantages. In addition, some competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments, and establish more relationships, than us. Current market conditions may attract more competitors, which may increase the competition for sources of financing. An increase in the competition for sources of funding could adversely affect the availability and cost of financing, and thereby adversely affect the market price of our common stock.

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Employees

Previous to January 1, 2014, other than our chief financial officer, we have had no employees and have been managed by our Manager pursuant to the Management Agreement between our Manager and us dated as of May 9, 2012. On January 1, 2014, our chief financial officer also became an employee of our Manager.

Corporate Governance and Internet Address

We emphasize the importance of professional business conduct and ethics through our corporate governance initiatives. In 2014 the Board took additional steps to enhance governance by appointing a lead independent director and adding a fourth independent director so that our Board of Directors consists of two thirds ($^2/_3$) independent directors. The audit, nominating and corporate governance, and compensation committees of our Board of Directors are composed entirely of independent directors. We have adopted corporate governance guidelines and a code of business conduct and ethics, which delineate our standards for our officers and directors.

Our internet address is www.westernassetmcc.com. The information on our website is not incorporated by reference in this Annual Report on Form 10-K. We make available, free of charge through a link on our site, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to such reports, if any, as filed or furnished with the SEC, as soon as reasonably practicable after such filing or furnishing. Our site also contains our code of business conduct and ethics, corporate governance guidelines and the charters of our audit committee, nominating and corporate governance committee and compensation committee of our Board of Directors. Within the time period required by the rules of the SEC and the New York Stock Exchange, or NYSE, we will post on our website any amendment to our code of business conduct and ethics as defined in the code. Our documents filed with, or furnished to, the SEC are also available for review and copying by the public at the SEC's Public Reference Room at 100 F Street, NE., Washington, DC 20549 and at the SEC's website at www.sec.gov. Information regarding the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330.

Item 1A. Risk Factors

Our business and operations are subject to a number of risks and uncertainties, the occurrence of which could adversely affect our business, financial condition, results of operations and ability to make distributions to stockholders and could cause the value of our capital stock to decline.

Risks related to our business

We have a limited operating history and may not be able to successfully operate our business or generate sufficient revenue to make or sustain distributions to our stockholders.

We were organized as a Delaware corporation on June 3, 2009, but did not commence operations until the completion of our IPO on May 15, 2012. We cannot assure you that we will be able to continue to operate our business successfully or implement our operating policies and strategies as described herein. The results of our operations depend on several factors, including the availability of opportunities for the acquisition of assets, the level and volatility of interest rates, the availability of adequate short and long-term financing, conditions in the financial markets and economic conditions.

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We may change any of our strategies, policies or procedures without stockholder consent.

We may change any of our strategies, policies or procedures with respect to investments, acquisitions, growth, operations, indebtedness, capitalization, distributions, financing strategy and leverage at any time without the consent of our stockholders, which could result in an investment portfolio with a different risk profile. A change in our investment strategy may increase our exposure to interest rate risk, default risk and real estate market fluctuations. Furthermore, a change in our asset allocation could result in our making investments in asset categories different from those described herein. These changes could adversely affect our financial condition, results of operations, the market price of our common stock and our ability to make distributions to our stockholders.

We may be unable to operate within the parameters that allow us to be excluded from regulation as a commodity pool operator, which would subject us to additional regulation and compliance requirements, and could materially adversely affect our business and financial condition.

As a result of regulatory changes prompted by the Dodd-Frank Act, any investment fund that trades in swaps may be considered a "commodity pool," which would cause its operators to be regulated as a "commodity pool operator" (or, CPO). In December 2012, the Commodity Futures Trading Commission issued a no-action letter giving relief to operators of mortgage REITs from the requirements applicable to CPOs. In order to qualify, we must, among other non-operation requirements: (1) limit our initial margin and premiums for commodity interests (swaps and exchange-traded futures) to no more than 5% of the fair market value of our total assets; and (2) limit our net income from commodity interests that are not "qualifying hedging transactions" to less than 5% of our gross income. These parameters could limit the use of swaps by us below the level that our Manager would otherwise consider optimal or may lead to the registration of our Manager or directors as commodity pool operators, which will subject us to additional regulatory oversight, compliance and costs.

Recent changes to derivatives regulation may increase the costs of hedging for the Company.

Recently, regulations have been promulgated by U.S. and foreign regulators attempting to strengthen oversight of derivative contracts. The Dodd-Frank Act established a comprehensive new regulatory framework for derivative contracts commonly referred to as "swaps" which requires that many swaps be executed on a regulated exchange or trading platform ("mandatory exchange trading") and cleared through a central counterparty ("mandatory clearing"). In particular, certain of the swaps that the Manager may want to use to hedge the Company's exposure to fluctuations in interest rates may now be subject to mandatory clearing and mandatory exchange trading. For swaps that are subject to mandatory clearing, the Company will be forced to pledge some of its assets to a clearing broker as initial margin, and for the life of such swaps, the assets pledged as initial margin generally will not be available to the Company for investment. For swaps that are subject to mandatory clearing and mandatory exchange trading, the Company likely will incur additional fees and costs for transactions in such swaps. Together, these requirements may make our Manager's hedging strategies more costly or may induce our Manager to change its hedging strategies.

In the past, our internal controls over financial reporting were found to have material weaknesses.

In conjunction with our 2012 audit, we determined that we had a material weakness in our internal control over financial reporting as of December 31, 2012. This material weakness was attributable to management's supervision, review and acceptance of procedures with respect to a third-party vendor's computation of interest income accretion and amortization of the cost basis of certain Agency RMBS. A detailed description of this material weakness was provided in Part II, Item 9A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2012. Due solely to this material weakness, we concluded that our disclosure controls and procedures as of December 31, 2012 were not effective.

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Beginning in the first quarter of 2013, we implemented a series of internal controls over financial reporting in order to remediate this issue, as described further in our quarterly reports on Form 10-Q for the quarters ended March 31, 2013, June 30, 2013 and September 30, 2013. During the third and fourth quarter of 2013, we tested each of the aforementioned procedures and based on the results of that testing we believe such procedures have been successfully implemented and have remediated the material weakness referenced above.

We may continue to expend significant financial resources and time in order to improve our internal controls over financial reporting.

We are responsible for establishing and maintaining adequate internal control over financial reporting designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. We cannot ensure you that there will not be any other material weaknesses in our internal control over financial reporting in the future.

Cybersecurity risk and cyber incidents may adversely affect our business by causing a disruption to our operations, a compromise or corruption of our confidential information and/or damage to our business relationships, all of which could negatively impact our financial results.

A cyber incident is considered to be any adverse event that threatens the confidentiality, integrity or availability of our information resources. These incidents may be an intentional attack or an unintentional event and could involve gaining unauthorized access to our information systems for purposes of misappropriating assets, stealing confidential information, corrupting data or causing operational disruption. The result of these incidents may include disrupted operations, misstated or unreliable financial data, liability for stolen assets or information, increased cybersecurity protection and insurance cost, litigation and damage to our investor relationships. As our reliance on technology has increased, so have the risks posed to both our information systems, both internal and those provided by our Manager and third-party service providers. Our Manager has implemented processes, procedures and internal controls to help mitigate cybersecurity risks and cyber intrusions, but these measures, as well as our increased awareness of the nature and extent of a risk of a cyber incident, do not guarantee that our financial results, operations or confidential information will not be negatively impacted by such an incident.

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Risks related to our investing strategy

Mortgage loan modification, refinancing programs, reduction in mortgage insurance premiums and minimum down payments and future legislative action may adversely affect the value of, and our returns on, Agency RMBS, Non-Agency RMBS and our additional Target Assets..

The U.S. Government, through the U.S. Federal Reserve, the Federal Housing Administration, or the FHA, and the Federal Deposit Insurance Corporation, has implemented a number of federal programs designed to assist homeowners, including the Home Affordable Modification Program, or HAMP, which provides homeowners with assistance in avoiding residential mortgage loan foreclosures, the Hope for Homeowners Program, or H4H Program, which allowed certain distressed borrowers to refinance their mortgages into FHA-insured loans in order to avoid residential mortgage loan foreclosures, and the Home Affordable Refinance Program, or HARP, which allows borrowers who are current on their mortgage payments to refinance and reduce their monthly mortgage payments at loan-to-value ratios up to 125% (and, in some cases, above 125%) without new mortgage insurance. A number of these homeowners' assistance programs have been enhanced or expanded and the HAMP and HARP programs have been extended through December 31, 2016. In addition, current administration officials and certain members of the U.S. Congress have indicated support for additional legislative relief for homeowners, including an amendment of the bankruptcy laws to permit the modification of mortgage loans in bankruptcy proceedings. Loan modifications are more likely to be used when borrowers are less able to refinance or sell their homes due to market conditions and when the potential recovery from a foreclosure is reduced due to lower property values. A significant number of loan modifications could result in a significant reduction in cash flows to the holders of the mortgage securities on an ongoing basis. Amendments to the bankruptcy laws that result in the modification of outstanding mortgage loans may adversely affect the value of and the returns on, the assets that we intend to acquire and the assets we currently hold.

Especially with Non-Agency RMBS, a significant number of loan modifications with respect to a given security, including, but not limited to, those related to principal forgiveness and coupon reduction, resulting in increased prepayment rates, could negatively impact the realized yields and cash flows on such security. These loan modification programs, future legislative or regulatory actions, including possible amendments to the bankruptcy laws, which result in the modification of outstanding residential mortgage loans, as well as changes in the requirements necessary to qualify for refinancing mortgage loans with FNMA, FHLMC or GNMA may adversely affect the value of, and the returns on, Agency RMBS and Non-Agency RMBS.

In October 2014, the FHA announced that it would allow FNMA and FHLMC to purchase loans with three percent (3%) down payments, thereby reducing the down payment requirement for borrowers to access mortgage loans which are eligible for purchase and/or guarantee by these U.S. Government sponsored entities or GSEs. Further, in January 2015, the Obama administration announced a 50 basis points (0.50%) reduction in the annual mortgage insurance premium imposed by the FHA on mortgage loans guaranteed by GNMA. The reduction in the minimum down payment along with lowering all-in mortgage interest rates on GSE sponsored residential mortgage loans will likely increase the attractiveness of refinancing as well as purchases of new and existing homes, thereby increasing the prepayment rates on the mortgage loans underlying our existing RMBS. This may adversely affect the value of, and the returns on, these assets, especially those which we acquired at a premium.

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The federal conservatorship of FNMA and FHLMC and related efforts, along with any changes in laws and regulations affecting the relationship between these agencies and the U.S. Government, may adversely affect our business.

The payments of principal and interest we receive on our Agency RMBS, which depend directly upon payments on the mortgages underlying such securities, are guaranteed by FNMA, FHLMC and GNMA. FNMA and FHLMC are U.S. Government-sponsored entities, or GSEs, but their guarantees are not backed by the full faith and credit of the United States. GNMA is part of a U.S. Government agency and its guarantees are backed by the full faith and credit of the United States.

In response to general market instability and, more specifically, the financial conditions of FNMA and FHLMC, in July 2008, the Housing and Economic Recovery Act of 2008, or HERA, established a new regulator for FNMA and FHLMC, the U.S. Federal Housing Finance Agency, or the FHFA. In September 2008, the U.S. Treasury, the FHFA and the U.S. Federal Reserve announced a comprehensive action plan to help stabilize the financial markets, support the availability of mortgage financing and protect taxpayers. Under this plan, among other things, the FHFA was appointed as conservator of both FNMA and FHLMC, allowing the FHFA to control the actions of the two GSEs, without forcing them to liquidate, which would be the case under receivership. Importantly, the primary focus of the plan was to increase the availability of mortgage financing by allowing these GSEs to continue to grow their guarantee business without limit, while limiting the size of their retained mortgage and Agency security portfolios and requiring that these portfolios be reduced over time.

Although the U.S. Government has committed to support the positive net worth of FNMA and FHLMC, there can be no assurance that these actions will be adequate for their needs. These uncertainties lead to questions about the availability of, and trading market for, Agency RMBS. Despite the steps taken by the U.S. Government, FNMA and FHLMC could default on their guarantee obligations which would materially and adversely affect the value of our Agency RMBS. Accordingly, if these government actions are inadequate and the GSEs continue to suffer losses or cease to exist, our business, operations and financial condition could be materially and adversely affected.

In addition, the problems faced by FNMA and FHLMC resulting in their being placed into federal conservatorship and receiving significant U.S. Government support have sparked serious debate among federal policy makers regarding the continued role of the U.S. Government in providing liquidity for mortgage loans. The future roles of FNMA and FHLMC could be significantly reduced and the nature of their guarantee obligations could be considerably limited relative to historical measurements. Any such changes to the nature of their guarantee obligations could redefine what constitutes an Agency security and could have broad adverse implications for the market and our business, operations and financial condition. If FNMA or FHLMC were eliminated, or their structures were to change radically (*i.e.*, limitation or removal of the guarantee obligation), or their market share reduced because of required price increases or lower limits on the loans they can guarantee, we could be unable to acquire additional Agency RMBS and our existing Agency RMBS could be materially and adversely impacted.

We could be negatively affected in a number of ways depending on the manner in which related events unfold for FNMA and FHLMC. We currently rely significantly on our Agency RMBS as collateral for our financings under our repurchase agreements. Any decline in its value, or perceived market uncertainty about its value, would make it more difficult for us to obtain financing on our Agency RMBS on acceptable terms or at all, or to maintain our compliance with the terms of any financing transactions. Further, the current support provided by the U.S. Treasury to FNMA and FHLMC, and any additional support it may provide in the future, could have the effect of lowering the interest rates we expect to receive from Agency RMBS, thereby tightening the spread between the interest we earn on our Agency RMBS and the cost of financing those assets. A reduction in the supply of Agency RMBS could also negatively affect the pricing of Agency RMBS by reducing the spread between the interest we earn on our investment portfolio of Agency RMBS and our cost of financing that portfolio.

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In March 2013, the U.S. Federal Housing Finance Agency announced that it would establish a new institutional body, which later became known as the Federal Mortgage Insurance Currency or, FMIC, to replace FNMA and FHLMC once they wind down operations. In June 2013, in a draft bill entitled the "Secondary Mortgage Market Reform and Taxpayer Protection Act of 2013" it was proposed that the FMIC would be modeled after the Federal Deposit Insurance Corporation or FDIC and provide catastrophic reinsurance in the secondary market for mortgage-backed securities. It would also take over multi-family guarantees as the existing portfolios of FNMA and FHLMC are wound down by at least 15% annually until they are completely liquidated. Future legislation affecting the Agencies may create market uncertainty and have the effect of reducing the actual or perceived credit quality of the Agencies and the securities issued or guaranteed by them. As a result, such laws could increase the risk of loss on our investments in Agency RMBS. It also is possible that such laws could adversely impact the market for such securities and the spreads at which they trade. All of the foregoing could have a material adverse effect on our business, financial condition, results of operations, the market price of our capital stock and our ability to pay dividends to our stockholders.

In December 2013, Representative Melvin L. Watt was confirmed as the director of the FHFA, replacing then acting director Edward J. DeMarco. Throughout his tenure, Mr. DeMarco repeatedly struck down various attempts regarding debt forgiveness for homeowners. A change in leadership at the FHFA may increase the likelihood of the implementation of such a program. A program which provides for debt forgiveness on the mortgages underlying our Agency RMBS is likely to have a negative impact on the value of our Agency RMBS, our ability to finance these securities and the interest income which we earn on such securities.

As provided above, recent legislation has changed the relationship between FNMA and FHLMC and the U.S. Government. The appointment of Representative Watt as director of the FHFA as well as future legislation could further change the relationship between FNMA and FHLMC and the U.S. Government which could also nationalize, privatize, or eliminate such entities entirely. In March 2014, Senate Banking Committee Chairman Tim Johnson and Ranking Member Mike Crapo announced an agreement on their own version of GSE reform which would eventually replace FNMA and FHLMC with a new system. Any law affecting these GSEs may create market uncertainty and have the effect of reducing the actual or perceived credit quality of securities issued or guaranteed by FNMA or FHLMC. Any law affecting these GSEs may create market uncertainty and have the effect of reducing the actual or perceived credit quality of securities issued or guaranteed by FNMA or FHLMC. As a result, such laws could increase the risk of loss on our investments in Agency RMBS guaranteed by FNMA and/or FHLMC. It also is possible that such laws could adversely impact the market for such securities and spreads at which they trade. All of the foregoing could materially and adversely affect our financial condition and results of operations.

We are subject to the risk that U.S. Government agencies and/or GSEs may not be able to fully satisfy their guarantees of Agency RMBS or that these guarantee obligations may be repudiated, which may adversely affect the value of our assets and our ability to sell or finance these securities.

The interest and principal payments we receive on the Agency RMBS in which we invest are guaranteed by FNMA, FHLMC or GNMA. Unlike the GNMA securities in which we may invest, the principal and interest on securities issued by FNMA and FHLMC are not guaranteed by the U.S. government. All the Agency RMBS in which we invest depend on a steady stream of payments on the mortgages underlying the securities.

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As conservator of FNMA and FHLMC, the FHFA may disaffirm or repudiate contracts (subject to certain limitations for qualified financial contracts) that FHLMC or FNMA entered into prior to the FHFA's appointment as conservator if it determines, in its sole discretion, that performance of the contract is burdensome and that disaffirmation or repudiation of the contract promotes the orderly administration of its affairs. The HERA requires the FHFA to exercise its right to disaffirm or repudiate most contracts within a reasonable period of time after its appointment as conservator. FNMA and FHLMC have disclosed that the FHFA has disaffirmed certain consulting and other contracts that these entities entered into prior to the FHFA's appointment as conservator. FHLMC and FNMA have also disclosed that the FHFA has advised that it does not intend to repudiate any guarantee obligation relating to FNMA's and FHLMC's mortgage-related securities, because the FHFA views repudiation as incompatible with the goals of the conservatorship. In addition, the HERA provides that mortgage loans and mortgage-related assets that have been transferred to a FHLMC or FNMA securitization trust must be held for the beneficial owners of the related mortgage-related securities, and cannot be used to satisfy the general creditors of FHLMC or FNMA.

If the guarantee obligations of FHLMC or FNMA were repudiated by the FHFA, payments of principal and/or interest to holders of Agency RMBS issued by FHLMC or FNMA would be reduced in the event of any borrowers' late payments or failure to pay or a servicer's failure to remit borrower payments to the trust. In that case, trust administration and servicing fees could be paid from mortgage payments prior to distributions to holders of Agency RMBS. Any actual direct compensatory damages owed due to the repudiation of FHLMC or FNMA's guarantee obligations may not be sufficient to offset any shortfalls experienced by holders of Agency RMBS. The FHFA also has the right to transfer or sell any asset or liability of FHLMC or FNMA, including its guarantee obligation, without any approval, assignment or consent. If the FHFA were to transfer FHLMC or FNMA's guarantee obligations to another party, holders of Agency RMBS would have to rely on that party for satisfaction of the guarantee obligation and would be exposed to the credit risk of that party.

In 2014, we invested in risk sharing securities issued by FNMA and FHLMC. Principal and interest payments on these securities are based on the performance of a specified pool of Agency residential mortgages. The payments due on these securities, however, are not secured by the referenced mortgages, but are full faith and credit obligations of Fannie Mae or Freddie Mac respectively. There is no implicit or explicit guarantee of these obligations by FHFA or that FHFA would satisfy such obligations if FNMA and/or FHLMC were to default.

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We operate in a highly competitive market for investment opportunities and competition may limit our ability to acquire desirable investments in our Target Assets and could also affect the pricing of these securities.

We operate in a highly competitive market for investment opportunities. Currently, our profitability depends, in large part, on our ability to acquire our Target Assets at attractive prices. In acquiring these assets, we compete with a variety of institutional investors, including other REITs, specialty finance companies, public and private funds (including other funds managed by our Manager), commercial and investment banks, commercial finance and insurance companies and other financial institutions. Many of our competitors are substantially larger and have considerably greater financial, technical, marketing and other resources than we do. Other REITs have recently raised, or may raise, additional capital, and may have investment objectives that overlap with ours, which may create additional competition for investment opportunities. Some competitors may have a lower cost of funds and access to funding sources that may not be available to us, such as funding from the U.S. Government. Many of our competitors are not subject to the operating constraints associated with REIT tax compliance or maintenance of an exemption from the 1940 Act. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more relationships than us. Furthermore, competition for investments in our Target Assets may lead to the price of such assets increasing, which may further limit our ability to generate desired returns. We cannot assure you that the competitive pressures we face will not have a material adverse effect on our business, financial condition and results of operations. Also, as a result of this competition, desirable investments in these assets may be limited in the future and we may not be able to take advantage of attractive investment opportunities from time to time, as we can provide no assurance that we will be able to identify and make investments that are consistent with our investment objectives.

A lack of liquidity in our investments may adversely affect our business.

The assets we acquire are not publicly traded. A lack of liquidity may result from the absence of a willing buyer or an established market for these assets, as well as legal or contractual restrictions on resale or the unavailability of financing for these assets. In addition, mortgage-related assets generally experience periods of illiquidity, especially during periods of economic stress such as the recent economic recession which resulted in increased delinquencies and defaults with respect to residential and commercial mortgage loans. The illiquidity of our investments may make it difficult for us to sell such investments if the need or desire arises. In addition, if we are required to liquidate all or a portion of our portfolio quickly, we may realize significantly less than the value at which we have previously recorded our investments. Further, we may face other restrictions on our ability to liquidate an investment in a business entity to the extent that we or our Manager has or could be attributed with material, non-public information regarding such business entity. As a result, our ability to vary our portfolio in response to changes in economic and other conditions may be relatively limited, which could adversely affect our results of operations and financial condition.

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Adverse developments in the broader residential mortgage market may adversely affect the value of the assets in which we invest.

Since 2007, the residential mortgage market in the United States has experienced a variety of unprecedented difficulties and changed economic conditions, including defaults, credit losses and liquidity concerns. Certain commercial banks, investment banks and insurance companies announced extensive losses from exposure to the residential mortgage market. These losses reduced financial industry capital, leading to reduced liquidity for some institutions. These factors have impacted investor perception of the risk associated with real estate-related assets, including Agency RMBS and other high-quality RMBS assets. As a result, values for RMBS assets, including some Agency RMBS and other AAA-rated RMBS assets, have experienced a certain amount of volatility. Further increased volatility and deterioration in the broader residential mortgage and RMBS markets may adversely affect the performance and market value of the Agency RMBS and Non-Agency RMBS in which we invest.

Our most significant investments are Agency RMBS and to a lesser extent Non-Agency RMBS and Agency and Non-Agency CMBS. We need to rely on our securities as collateral for our financings. Any decline in their value, or perceived market uncertainty about their value, would likely make it difficult for us to obtain financing on favorable terms or at all, or maintain our compliance with terms of any financing arrangements already in place. The securities we acquire are classified for accounting purposes as available-for-sale. All assets classified as available-for-sale are reported at fair value, based on market prices from third-party sources. We have elected to include any unrealized gains and losses in our earnings. If market conditions result in a decline in the fair value of our assets, our financial position and results of operations could be adversely affected.

A prolonged economic recession and further declining real estate values could impair our assets and harm our operations.

The risks associated with our business are more severe during economic recessions and are compounded by declining real estate values. The Non-Agency RMBS and Non-Agency CMBS in which we invest a part of our capital will be particularly sensitive to these risks. Declining real estate values will likely reduce the level of new mortgage loan originations since borrowers often use appreciation in the value of their existing properties to support the purchase of additional properties. Borrowers will also be less able to pay principal and interest on loans underlying the securities in which we invest if the value of residential and commercial real estate weakens further. Further, declining real estate values significantly increase the likelihood that we will incur losses on Non-Agency RMBS and Non-Agency CMBS in the event of default because the value of collateral on the mortgages underlying such securities may be insufficient to cover the outstanding principal amount of the loan. Any sustained period of increased payment delinquencies, foreclosures or losses could adversely affect our net interest income from Non-Agency RMBS and Non-Agency CMBS in our portfolio, which could have an adverse effect on our financial condition, results of operations and our ability to make distributions to our stockholders.

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Our investments are subject to a significant change in prepayments speeds affecting the value of our portfolio and possibly adversely affecting yields.

The value of our assets may be affected by prepayment rates on residential mortgage loans. We acquire RMBS and anticipate that the underlying residential mortgages loans will prepay at a projected rate generating an expected yield. If we purchase assets at a premium to par value, when borrowers prepay their residential mortgage loans faster than expected, the corresponding prepayments on the mortgage-related securities may reduce the expected yield on such securities because we will have to amortize the related premium on an accelerated basis. In the case of Agency RMBS whole pools and certain other investment grade rated securities, we will be required to make a retrospective adjustment to historical amortization. Conversely, if we purchase assets at a discount to par value, when borrowers prepay their residential mortgage loans slower than expected, the decrease in corresponding prepayments on the RMBS may reduce the expected yield on such securities because we will not be able to accrete the related discount as quickly as originally anticipated and, in the case of Agency RMBS whole pools and certain other investment grade rated securities, we will have to make a retrospective adjustment to historical amortization.

Commercial mortgages frequently limit the ability of the borrower to prepay, thereby providing a certain level of prepayment protection. Common restrictions include yield maintenance and prepayment penalties, the proceeds of which are generally at least partially allocable to these securities, as well as defeasance.

Our investments in Non-Agency RMBS are generally subject to losses.

In general, losses on a mortgaged property securing a mortgage loan included in a securitization will be borne first by the equity holder of the property, then by a cash reserve fund or letter of credit, if any, then by the holder of a mezzanine loan or B-Note, if any, then by the "first loss" subordinated security holder and then by the holder of a higher-rated security. In the event of default and the exhaustion of any equity support, reserve fund, letter of credit, mezzanine loans or B-Notes, and any classes of securities junior to those in which we invest, we will not be able to recover all of our investment in the securities we purchase. In addition, if the underlying mortgage portfolio has been overvalued by the originator, or if the values subsequently decline, less collateral is available to satisfy interest and principal payments due on the related Non-Agency RMBS. The prices of lower credit quality securities are generally less sensitive to interest rate changes than more highly rated investments, but more sensitive to adverse economic downturns or individual issuer developments.

The mortgage loans underlying the Non-Agency RMBS that we invest in will be subject to defaults, foreclosure timeline extension, fraud and residential price depreciation and unfavorable modification of loan principal amount, interest rate and amortization of principal, which could result in losses to us.

Our investments in Non-Agency RMBS are subject to the risks of defaults, foreclosure timeline extension, fraud and home price depreciation and unfavorable modification of loan principal amount, interest rate and amortization of principal, accompanying the underlying residential mortgage loans. The ability of a borrower to repay a mortgage loan secured by a residential property is dependent upon the income or assets of the borrower. A number of factors may impair borrowers' abilities to repay their loans, including:

- adverse changes in national and local economic and market conditions;
- changes in governmental laws and regulations, fiscal policies and zoning ordinances and the related costs of compliance with laws and regulations, fiscal policies and ordinances;
- costs of remediation and liabilities associated with environmental conditions such as indoor mold;
- the potential for uninsured or under-insured property losses;

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- acts of God, including earthquakes, floods and other natural disasters, which may result in uninsured losses; and

- acts of war or terrorism, including the consequences of terrorist attacks, such as those that occurred on September 11, 2001.

In the event of defaults on the residential mortgage loans that underlie our investments in Non-Agency RMBS and the exhaustion of any underlying or any additional credit support, we may not realize our anticipated return on our investments and we may incur a loss on these investments. In addition, our investments in Non-Agency RMBS will be backed by residential real property but, in contrast to Agency RMBS, the principal and interest will not be guaranteed by a U.S. Government agency or a GSE. The ability of a borrower to repay these loans or other financial assets is dependent upon the income or assets of these borrowers.

We may be affected by deficiencies in foreclosure practices of third parties, as well as related delays in the foreclosure process.

Allegations of deficiencies in foreclosure documentation and servicing and foreclosure practices by several large mortgage servicers have raised various concerns relating to foreclosure practices. As a result of these alleged deficiencies in foreclosure practices, a number of servicers temporarily suspended foreclosure proceedings beginning in the second half of 2010 while they evaluated their foreclosure practices. In addition, on February 9, 2012, a group consisting of state attorneys general and state bank and mortgage regulators in 49 states reached a settlement with the largest mortgage servicers regarding foreclosure practices in the states' various jurisdictions. On January 7, 2013, the Office of the Comptroller of the Currency and the Board of Governors of the Federal Reserve System announced a settlement with a number of mortgage servicers in lieu of continuing a foreclosure review process, under which borrowers who believed they were financially harmed by the foreclosure process in 2009 and 2010 were able to request an independent review of the process. The settlement, which includes funds for both direct payments to eligible borrowers and for other assistance such as loan modifications and forgiveness of deficiency judgments, ended the case-by-case reviews. Although servicers have generally ended their suspension of foreclosures, the processing of foreclosures continues to be slow in many states due to continuing issues in the servicer foreclosure process, including efforts by servicers to comply with regulatory consent orders and requirements, recent changes in the state foreclosure laws, court rules and proceedings and the pipeline of foreclosures resulting from these delays as well as the elevated level of foreclosures caused by the housing market downturn. We may incur substantial legal fees and court costs in acquiring a property through contested foreclosure or bankruptcy proceedings. We intend to continue to monitor and review the issues raised by the alleged improper foreclosure practices.

Prior to making investments in RMBS, our Manager carefully considers many factors, including housing prices and foreclosure timelines, and estimate loss assumptions. The concerns about deficiencies in foreclosure practices of servicers and related delays in the foreclosure process may impact our loss assumptions and affect the values of, and our returns on, our investments in RMBS. We cannot predict exactly how the servicing and foreclosure matters or the resulting litigation or settlement agreements will affect our business and cannot assure you that these matters will not impair our performance and reduce the return on our investments.

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The commercial mortgage loans underlying the CMBS we may acquire will be subject to defaults, foreclosure timeline extension, fraud and commercial price depreciation and unfavorable modification of loan principal amount, interest rate and amortization of principal, which could result in losses to us.

CMBS may be secured by a single commercial mortgage loan or a pool of commercial mortgage loans. Commercial mortgage loans may be secured by multifamily or commercial property and are subject to risks of delinquency and foreclosure, and risks of loss that may be greater than similar risks associated with loans made on the security of residential property. The ability of a borrower to repay a loan secured by an income-producing property typically is dependent primarily upon the successful operation of such property rather than upon the existence of independent income or assets of the borrower. If the net operating income of the property is reduced, the borrower's ability or willingness to repay the loan may be impaired. Net operating income of an income-producing property can be affected by, among other things,

- tenant mix;
- success of tenant businesses;
- property management decisions;
- property location and condition;
- competition from comparable types of properties;
- changes in laws that increase operating expenses or limit rents that may be charged;
- any need to address environmental contamination at the property or the occurrence of any uninsured casualty at the property;
- changes in national, regional or local economic conditions and/or specific industry segments;
- declines in regional or local real estate values;
- declines in regional or local rental or occupancy rates;
- increases in interest rates;
- real estate tax rates and other operating expenses;
- changes in governmental rules, regulations and fiscal policies, including environmental legislation; and
- acts of God, terrorist attacks, social unrest and civil disturbances.

If our Manager overestimates the loss-adjusted yields of our CMBS investments, we may experience losses.

Our Manager will analyze any CMBS investments we may acquire based on loss-adjusted yields, taking into account estimated future losses on the mortgage loans included in the securitization's pool of loans, and the estimated impact of these losses on expected future cash flows. Our Manager's loss estimates may not prove accurate, as actual results may vary from estimates. In the event that our Manager underestimates the pool level losses relative to the price we pay for a particular CMBS investment, we may experience losses with respect to such investment.

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We do not control the special servicing of the mortgage loans included in the CMBS in which we invest and, in such cases, the special servicer may take actions that could adversely affect our interests.

With respect to CMBS in which we invest, overall control over the special servicing of the related underlying mortgage loans will be held by a "directing certificateholder" or a "controlling class representative," which is appointed by the holders of the most subordinate class of CMBS in such series. We may not have the right to appoint the directing certificateholder. In connection with the servicing of the specially serviced mortgage loans, the related special servicer may, at the direction of the directing certificateholder, take actions with respect to the specially serviced mortgage loans that could adversely affect our interests.

The residential and/or commercial mortgages which we may acquire in the form of whole-loans are subject to individual borrower credit risk.

To the extent we acquire residential or commercial first lien mortgages or whole-loans; we will be subject to individual credit risk. While such mortgages will be secured by the single family residences or commercial properties, we will rely on the borrower's willingness to make timely payments. In certain states our ability to recover against a borrower on a residential property may be limited to either recovering from the borrower or foreclosing on the property. In either case, depending on state and local laws, such recovery could take an extended period of time and expense, during which period we would not be receiving any payments, thereby negatively impacting our cash flow. Similarly, to the extent a commercial loan is non-recourse, our recovery will be limited to the underlying real property which depending on several factors, including the location of such property, could take an extended period of time and expense, thereby negatively impacting our cash flow.

The receivables underlying the ABS we may acquire are subject to credit exposure, which could result in losses to us.

ABS are securities backed by various asset classes including auto loans, student loans, credit card loans, equipment loans, floor plan loans and small business loans fully guaranteed as to principal and interest by the U.S. Small Business Administration, or the SBA. ABS remain subject to the credit exposure of the underlying receivables. In the event of increased rates of delinquency with respect to any receivables underlying our ABS, we may not realize our anticipated return on these investments.

Our investments are recorded at fair value, and quoted prices or observable inputs may not be available to determine such value, resulting in the use of significant unobservable inputs to determine value.

We expect that the values of some of our investments may not be readily determinable. We measure the fair value of these investments on at least a monthly basis. The fair value at which our assets are recorded may not be an indication of their realizable value. Ultimate realization of the value of an asset depends to a great extent on economic and other conditions that are beyond the control of our Manager, our Company or our Board of Directors. Further, fair value is only an estimate based on good faith judgment of the price at which an investment can be sold since market prices of investments can only be determined by negotiation between a willing buyer and seller. If we were to liquidate a particular asset, the realized value may be more than or less than the amount at which such asset is valued. Accordingly, the value of our common stock could be adversely affected by our determinations regarding the fair value of our investments, whether in the applicable period or in the future. Additionally, such valuations may fluctuate over short periods of time.

Our determination of the fair value of our investments for GAAP includes inputs provided by third-party dealers and pricing services. Valuations of certain investments in which we invest are often difficult to obtain. In general, dealers and pricing services heavily disclaim their valuations. Dealers may claim to furnish valuations only as an accommodation and without special compensation, and so they may disclaim any and all liability for any direct, incidental, or consequential damages arising out of any inaccuracy or incompleteness in valuations, including any act of negligence or breach of any warranty. Depending on the complexity and illiquidity of a security, valuations of the same security can vary substantially from one dealer or pricing service to another. Therefore, our results of operations for a given period could be adversely affected if our determinations regarding the fair market value of these investments are materially different than the values that we ultimately realize upon their disposal. Due to an overall increase in market volatility, the valuation process has been particularly challenging recently as market events have made valuations of certain assets more difficult, unpredictable and volatile.

Declines in value of the assets in which we invest will adversely affect our financial position and results of operations, and make it more costly to finance these assets.

We use our investments as collateral for our financings. Any decline in their value, or perceived market uncertainty about their value, would likely make it difficult for us to obtain financing on favorable terms or at all, or maintain our compliance with terms of any financing arrangements already in place. Our investments in mortgage-backed securities are recorded at fair value under a fair value option election at the time of purchase with changes in fair value reported in earnings. As a result, a decline in fair values of our mortgage-backed securities could reduce both our earnings and stockholders' equity. If market conditions result in a decline in the fair value of our assets, our financial position and results of operations could be adversely affected.

An increase in interest rates may cause a decrease in the availability of certain of our Target Assets, which could adversely affect our ability to acquire assets that satisfy our investment objectives and to generate income and make distributions.

Rising interest rates generally reduce the demand for mortgage loans due to the higher cost of borrowing. A reduction in the volume of mortgage loans originated may affect the volume of our Target Assets available to us, which could adversely affect our ability to acquire assets that satisfy our investment objectives. Rising interest rates may also cause our assets that were issued prior to an interest rate increase to provide yields that are below prevailing market interest rates. If rising interest rates cause us to be unable to acquire a sufficient volume of our Target Assets with a yield that is above our borrowing cost, our ability to satisfy our investment objectives and to generate income and make distributions may be materially and adversely affected.

The relationship between short-term and longer-term interest rates is often referred to as the "yield curve." Ordinarily, short-term interest rates are lower than longer-term interest rates. If short-term interest rates rise disproportionately relative to longer-term interest rates (a flattening of the yield curve), our borrowing costs may increase more rapidly than the interest income earned on our assets. Because our investments, on average, generally bear interest based on longer-term rates than our borrowings, a flattening of the yield curve would tend to decrease our net income and the market value of our net assets. Additionally, to the extent cash flows from investments that return scheduled and unscheduled principal are reinvested, the spread between the yields on the new investments and available borrowing rates may decline, which would likely decrease our net income. It is also possible that short-term interest rates may exceed longer-term interest rates (a yield curve inversion); in which event our borrowing costs may exceed our interest income and we could incur operating losses.

Increases in interest rates could adversely affect the value of our investments and cause our interest expense to increase, which could result in reduced earnings or losses and negatively affect our profitability as well as the cash available for distribution to our stockholders.

We invest in Agency RMBS and Non-Agency RMBS. We also invest in Agency and Non-Agency CMBS and ABS. In a normal yield curve environment, investments in such assets will generally decline in value if long-term interest rates increase. Declines in market value may ultimately reduce earnings or result in losses to us, which may negatively affect cash available for distribution to our stockholders.

A significant risk associated with our Target Assets is the risk that both long-term and short-term interest rates will increase significantly. If long-term rates increased significantly, the market value of these investments would decline, and the duration and weighted average life of the investments would increase. We could realize a loss if the securities were sold. At the same time, an increase in short-term interest rates would increase the amount of interest owed on any repurchase agreements we may enter into, thereby potentially reducing the net interest margin we earn our investments and the income available for distribution to our shareholders.

Market values of our investments may decline without any general increase in interest rates for a number of reasons, such as increases or expected increases in defaults, or increases or expected increases in voluntary prepayments for those investments that are subject to prepayment risk or widening of credit spreads.

In addition, our operating results depend in large part on the difference between the income from our assets and our financing costs. We anticipate that, in most cases in a period of rising interest rates, the income from such assets will respond more slowly to interest rate fluctuations than the cost of our borrowings. Consequently, changes in interest rates, particularly short-term interest rates, may significantly influence our net income. Increases in these rates will tend to decrease our net income and market value of our assets.

Interest rate mismatches between our RMBS backed by ARMs or hybrid ARMs and our borrowings used to fund our purchases of these assets may cause us to suffer losses.

We may fund our RMBS with borrowings that have interest rates that adjust more frequently than the interest rate indices and repricing terms of RMBS backed by adjustable-rate mortgages, or ARMs, or hybrid ARMs. Accordingly, if short-term interest rates increase, our borrowing costs may increase faster than the interest rates on RMBS backed by ARMs or hybrid ARMs adjust. As a result, in a period of rising interest rates, we could experience a decrease in net income or a net loss.

In most cases, the interest rate indices and repricing terms of RMBS backed by ARMs or hybrid ARMs and our borrowings will not be identical, thereby potentially creating an interest rate mismatch between our investments and our borrowings. While the historical spread between relevant short-term interest rate indices has been relatively stable, there have been periods when the spread between these indices was volatile. During periods of changing interest rates, these interest rate index mismatches could reduce our net income or produce a net loss, and adversely affect the level of our dividends and the market price of our common stock.

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In addition, RMBS backed by ARMs or hybrid ARMs will typically be subject to lifetime interest rate caps that limit the amount an interest rate can increase through the maturity of the RMBS. However, our borrowings under repurchase agreements typically are not subject to similar restrictions. Accordingly, in a period of rapidly increasing interest rates, the interest rates paid on our borrowings could increase without limitation while caps could limit the interest rates on these types of RMBS. This problem is magnified for RMBS backed by ARMs or hybrid ARMs that are not fully indexed. Further, some RMBS backed by ARMs or hybrid ARMs may be subject to periodic payment caps that result in a portion of the interest being deferred and added to the principal outstanding. As a result, we may receive less cash income on these types of RMBS than we need to pay interest on our related borrowings. These factors could reduce our net interest income and cause us to suffer a loss during periods of rising interest rates.

As of December 31, 2014, none of our Agency RMBS, excluding Interest-Only Strips, were secured by ARMs or hybrid ARMs. Our Non-Agency RMBS, however, were secured by ARMs, Hybrid ARMS, pay option ARMs and fixed-rate mortgages. Further, there can be no assurance that this will not change in the future.

Interest rate fluctuations may adversely affect the level of our net income and the value of our assets and common stock.

Interest rates are highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors beyond our control. Interest rate fluctuations present a variety of risks, including the risk of a narrowing of the difference between asset yields and borrowing rates, flattening or inversion of the yield curve and fluctuating prepayment rates, and may adversely affect our income and the value of our assets and common stock.

Increases in interest rates may negatively affect the market value of the fixed-rate mortgages and hybrid ARMs in which we may invest. Our investments in these mortgage-backed securities are recorded at fair value under a fair value option election at the time of purchase with changes in fair value reported in earnings and any decrease in our earnings could cause the market value of our common stock to decline. In addition, rising interest rates generally reduce the demand for consumer and commercial credit, including mortgage loans, due to the higher cost of borrowing. A reduction in the volume of mortgage loans originated may affect the volume of MBS available to us, which could affect our ability to acquire assets that satisfy our investment objectives.

Since the onset of the economic recession in 2008, the Federal Reserve has maintained an accommodative monetary policy. Recent improvements in the U.S. labor market and overall U.S. economy has led to a discussion of the return of monetary policy to a more "normal" stature. In the press release issued subsequent to the Federal Open Market Committee on January 27 and 28, 2015, the Federal Reserve reaffirmed its view that the current 0% to 0.25% target range for the federal funds rate is appropriate as it works to support continued progress toward its dual goal of maximum employment and price stability. While not providing a definitive time frame for when it expects to begin raising short term interest rates, the Federal Reserve reiterated that it can remain patient in beginning to normalize monetary policy and that such actions will be driven by economic data. Accordingly, we cannot project with certainty when and the rate at which the Federal Reserve will increase the Federal Funds rate and what impact that will have on our business and operating results.

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Changes in prepayment rates may adversely affect our profitability.

The RMBS assets we acquire are backed by pools of residential mortgage loans. We receive payments, generally, from the payments that are made on these underlying residential mortgage loans. While commercial mortgages frequently include limitations on the ability of the borrower to prepay, residential mortgages generally do not. When borrowers prepay their residential mortgage loans at rates that are faster than expected, the net result is prepayments that are faster than expected on the related RMBS. These faster than expected payments may adversely affect our profitability.

We may purchase RMBS assets that have a higher interest rate than the then prevailing market interest rate. In exchange for this higher interest rate, we may pay a premium to par value to acquire the asset. In accordance with accounting rules, we amortize this premium over the expected term of the asset based on our prepayment assumptions. If the asset is prepaid in whole or in part at a faster than expected rate, however, we must expense all or a part of the remaining unamortized portion of the premium that was paid at the time of the purchase, which will adversely affect our profitability.

Prepayment rates generally increase when interest rates fall and decrease when interest rates rise, but changes in prepayment rates are difficult to predict. House price appreciation, while increasing the value of the collateral underlying our RMBS, may increase prepayment rates as borrowers may be able to refinance at more favorable terms. Prepayments can also occur when borrowers default on their residential mortgages and the mortgages are prepaid from the proceeds of a foreclosure sale of the property (an involuntary prepayment), or when borrowers sell the property and use the sale proceeds to prepay the mortgage as part of a physical relocation. Prepayment rates also may be affected by conditions in the housing and financial markets, increasing defaults on residential mortgage loans, which could lead to an acceleration of the payment of the related principal, general economic conditions and the relative interest rates on fixed-rate mortgages and ARMs. While we seek to manage prepayment risk, in selecting RMBS investments we must balance prepayment risk against other risks, the potential returns of each investment and the cost of hedging our risks. No strategy can completely insulate us from prepayment or other such risks, and we may deliberately retain exposure to prepayment or other risks.

In addition, a decrease in prepayment rates may adversely affect our profitability. When borrowers prepay their residential mortgage loans at slower than expected rates, prepayments on the RMBS may be slower than expected. These slower than expected payments may adversely affect our profitability. We may purchase RMBS assets that have a lower interest rate than the then prevailing market interest rate. In exchange for this lower interest rate, we may pay a discount to par value to acquire the asset. In accordance with accounting rules, we accrete this discount over the expected term of the asset based on our prepayment assumptions. If the asset is prepaid at a slower than expected rate, however, we must accrete the remaining portion of the discount at a slower than expected rate. This will extend the expected life of the asset and result in a lower than expected yield on assets purchased at a discount to par.

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We may make investments in non-U.S. dollar denominated securities, which will be subject to currency rate exposure and risks associated with the uncertainty of foreign laws and markets.

Some of our real estate-related securities investments may be denominated in foreign currencies, and therefore, we expect to have currency risk exposure to any such foreign currencies. A change in foreign currency exchange rates may have an adverse impact on returns on our non-U.S. dollar denominated investments. Although we may hedge our foreign currency risk subject to the REIT income tests, we may not be able to do so successfully and may incur losses on these investments as a result of exchange rate fluctuations. To the extent that we invest in non-U.S. dollar denominated securities, in addition to risks inherent in the investment in securities generally discussed in this Form 10-K, we will also be subject to risks associated with the uncertainty of foreign laws and markets including, but not limited to, unexpected changes in regulatory requirements, political and economic instability in certain geographic locations, difficulties in managing international operations, currency exchange controls, potentially adverse tax consequences, additional accounting and control expenses and the administrative burden of complying with a wide variety of foreign laws.

We are highly dependent on information systems and systems failures could significantly disrupt our business, which may, in turn, negatively affect the market price of our common stock and our ability to make distributions to all stockholders.

Our business is highly dependent on communications and information systems of our Manager and other third-party service providers. Any failure or interruption of our Manager's or other third-party service providers' systems could cause delays or other problems in our securities trading activities, which could have a material adverse effect on our operating results and negatively affect the market price of our common stock and our ability to make distributions to our stockholders.

Loss of our exemption from regulation pursuant to the 1940 Act would adversely affect us.

We conduct our business so as not to become regulated as an investment company under the 1940 Act in reliance on the exemption provided by Section 3(c)(5)(C) of the 1940 Act. Section 3(c)(5)(C), as interpreted by the staff of the SEC, requires that: (i) at least 55% of our investment portfolio consist of "mortgages and other liens on and interest in real estate," or "qualifying real estate interests," and (ii) at least 80% of our investment portfolio consist of qualifying real estate interests plus "real estate-related assets." In satisfying this 55% requirement, based on pronouncements of the SEC staff, we may treat whole pool Agency RMBS as qualifying real estate interests. The SEC staff has not issued guidance with respect to whole pool Non-Agency RMBS. Accordingly, based on our own judgment and analysis of the SEC's pronouncements with respect to whole pool Agency RMBS, we may also treat Non-Agency RMBS issued with respect to an underlying pool of mortgage loans in which we hold all of the certificates issued by the pool as qualifying real estate interests. We currently treat partial pool Agency, Non-Agency RMBS and partial pool CMBS as real estate-related assets. We treat any interest rate swaps or other derivative hedging transactions we enter into as miscellaneous assets that will not exceed 20% of our total assets. We rely on guidance published by the SEC staff or on our analyses of guidance published with respect to other types of assets to determine which assets are qualifying real estate assets and real estate-related assets.

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The SEC in 2011 solicited public comment on a wide range of issues relating to Section 3(c)(5)(C), including the nature of the assets that qualify for purposes of the exemption and whether mortgage REITs should be regulated in a manner similar to investment companies. To date the staff has not issued any additional guidance. There can be no assurance that the laws and regulations governing the 1940 Act status of REITs, including the guidance of the Division of Investment Management of the SEC regarding this exemption, will not change in a manner that adversely affects our operations. To the extent that the SEC or its staff publishes new or different guidance with respect to these matters, we may be required to adjust our strategy accordingly. In addition, we may be limited in our ability to make certain investments and these limitations could require us to hold assets we might wish to sell or to sell assets we might wish to hold. To the extent that the SEC staff provides more specific guidance regarding any of the matters bearing upon the exemption we rely on from the 1940 Act, we may be required to adjust our strategy accordingly. Any additional guidance from the SEC staff could provide additional flexibility to us, or it could further inhibit our ability to pursue the strategies we have chosen.

The mortgage related investments that we acquire are limited by the provisions of the 1940 Act and the rules and regulations promulgated thereunder. If the SEC determines that any of these securities are not qualifying interests in real estate or real estate-related assets, adopts a contrary interpretation with respect to these securities or otherwise believes we do not satisfy the above exceptions or changes its interpretation of the above exceptions, we could be required to restructure our activities or sell certain of our assets. We may be required at times to adopt less efficient methods of financing certain of our mortgage related investments and we may be precluded from acquiring certain types of higher yielding securities. The net effect of these factors would be to lower our net interest income. If we fail to qualify for an exemption from registration as an investment company or an exclusion from the definition of an investment company, our ability to use leverage would be substantially reduced. Further, if the SEC determined that we were an unregistered investment company, we could be subject to monetary penalties and injunctive relief in an action brought by the SEC, we would potentially be unable to enforce contracts with third parties which could seek to obtain rescission of transactions undertaken during the period for which it was established we were an unregistered investment company. If we were required to register as an investment company, it would result in a change of our financial statement requirements. Our business will be materially and adversely affected if we fail to qualify for this exemption from regulation pursuant to the 1940 Act. In addition, the loss of our 1940 Act exemption would also permit our Manager to terminate the Management Agreement, which could result in material adverse effect on our business and results of operations.

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The downgrade of the U.S. government's or certain European countries' credit ratings and any future downgrades of the U.S. government's or certain European countries' credit ratings may materially adversely affect our business, financial condition and results of operations.

On August 5, 2011, Standard & Poor's downgraded the U.S. government's credit rating for the first time in history. More recently, concerns over economic recession, geopolitical issues, the ability of certain European sovereigns to honor their debt obligations and the exposure of certain European financial institutions to such debt, potential deflationary pressures in Europe, slowing growth in China, rapid decline in the price of oil and certain other commodities, the availability and cost of financing, the mortgage market, uncertainty related to political events such as the government spending and tax policy and uncertain real estate market have contributed to volatility and relatively low expectations for the world economy and domestic and international markets. Because FNMA and FHLMC are in conservatorship of the U.S. government, downgrades to the U.S. government's credit rating could impact the credit risk associated with Agency MBS and, therefore, decrease the value of the Agency MBS in which we invest. In addition, the downgrade of the U.S. government's credit rating and the credit ratings of certain European countries has created broader financial turmoil and uncertainty, which has recently weighed heavily on the global banking system. Therefore, the downgrade of the U.S. government's credit rating and the credit ratings of certain European countries and any future downgrades of the U.S. government's credit rating or the credit rating s of certain European countries may materially adversely affect our business, financial condition and results of operations.

Risks related to financing and hedging

Our strategy involves significant leverage, which may amplify losses.

Our current target leverage generally ranges between five to ten times the amount of our stockholders' equity (calculated in accordance with U.S. GAAP). We incur this leverage by borrowing against a substantial portion of the market value of our assets. By utilizing this leverage, we can enhance our returns. Nevertheless, this leverage, which is fundamental to our investment strategy, also creates significant risks.

As a result of our significant leverage, we may incur substantial losses if our borrowing costs increase. Our borrowing costs may increase for any of the following reasons:

- short-term interest rates increase;
- the market value of our securities decreases;
- interest rate volatility increases; or
- the availability of financing in the market decreases.

There can be no assurance that our Manager will be able to prevent mismatches in the maturities of our assets and liabilities.

Because we employ financial leverage in funding our portfolio, mismatches in the maturities of our assets and liabilities can create risk in the need to continually renew or otherwise refinance our liabilities. Our net interest margins are dependent upon a positive spread between the returns on our asset portfolio and our overall cost of funding. Our Manager actively employs portfolio-wide and security-specific risk measurement and management processes in our daily operations. Our Manager's risk management tools include software and services licensed or purchased from third parties, in addition to proprietary systems and analytical methods developed internally. There can be no assurance that these tools and the other risk management techniques described above will protect us from asset/liability risks.

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We may be subject to margin calls under our master repurchase agreements, which could result in defaults or force us to sell assets under adverse market conditions or through foreclosure.

We have entered into master repurchase agreements with various financial institutions and borrow under these master repurchase agreements to finance the acquisition of assets for our investment portfolio. Pursuant to the terms of borrowings under our master repurchase agreements, a decline in the value of the subject assets may result in our lenders initiating margin calls. A margin call means that the lender requires us to pledge additional collateral to re-establish the ratio of the value of the collateral to the amount of the borrowing. The specific collateral value to borrowing ratio that would trigger a margin call is not set in the master repurchase agreements and will not be determined until we engage in a repurchase transaction under these agreements. Our fixed-rate securities generally are more susceptible to margin calls as increases in interest rates tend to have a greater negative affect on the market value of fixed-rate securities. If we are unable to satisfy margin calls, our lenders may foreclose on our collateral. The threat of or occurrence of a margin call could force us to sell our assets, either directly or through a foreclosure, under adverse market conditions. Because of the significant leverage we have, we may incur substantial losses upon the threat or occurrence of a margin call.

If a counterparty to our repurchase transactions defaults on its obligation to resell the underlying security back to us at the end of the transaction term, or if the value of the underlying security has declined as of the end of that term, or if we default on our obligations under the repurchase agreement, we will lose money on our repurchase transactions.

When we engage in repurchase transactions, we generally sell securities to lenders (repurchase agreement counterparties) and receive cash from these lenders. The lenders are obligated to resell the same securities back to us at the end of the term of the transaction. Because the cash we receive from the lender when we initially sell the securities to the lender will be less than the value of those securities (this difference is the haircut), if the lender defaults on its obligation to resell the same securities back to us we may incur a loss on the transaction equal to the amount of the haircut (assuming there was no change in the value of the securities). We would also lose money on a repurchase transaction if the value of the underlying securities has declined as of the end of the transaction term, as we would have to repurchase the securities based on their initial value but would receive securities worth less than that amount. Further, if we default on one of our obligations under a repurchase transaction, the lender can terminate the transaction and cease entering into any other repurchase transactions with us. Our inability to post adequate collateral for a margin call by the counterparty, in a timeframe as short as the close of the same business day, could result in a condition of default under our repurchase agreements, thereby enabling the counterparty to liquidate the collateral pledged by us, which may have a material adverse effect on our financial position, results of operations and cash flows. Our repurchase agreements contain cross-default provisions, such that if a default occurs under an agreement with any specific lender, that lender could also declare a default under other repurchase agreements or other financing or derivative contracts, if any, with such lender. Further, 19 of the counterparties to our repurchase agreements held, as of December 31, 2014, collateral valued in excess of 5% of our stockholders' equity as security for our obligations under the applicable repurchase agreements. Any losses we incur on our repurchase transactions could adversely affect our earnings and thus our cash available for distribution to our stockholders.

If a counterparty to one of our swap agreements or TBAs defaults on its obligations, we may incur losses.

If a counterparty to one of the bilateral swap agreements that we enter into or TBAs that we enter into defaults on its obligations under the agreement, we may not receive payments due under the agreement, and thus, we may lose any unrealized gain associated with the agreement. In the case of a swap agreement, the fact that such swap agreement hedged a liability means that the liability could cease to be hedged upon the default of a counterparty. Additionally, we may also risk the loss of any collateral we have pledged to secure our obligations under a bilateral swap agreement if the counterparty, or in the case of a cleared swap, if our clearing broker, becomes insolvent or files for bankruptcy.

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Failure to procure adequate repurchase agreement financing, which generally have short terms, or to renew or replace repurchase agreement financing as it matures, would adversely affect our results of operations.

We use repurchase agreement financing as a strategy to increase the return on our investment portfolio. However, we may not be able to achieve our desired leverage ratio for a number of reasons, including if the following events occur:

- our lenders do not make repurchase agreement financing available to us at acceptable rates;
- certain of our lenders exit the repurchase market;
- our lenders require that we pledge additional collateral to cover our borrowings, which we may be unable to do; or
- we determine that the leverage would expose us to excessive risk.

We cannot assure you that any, or sufficient, repurchase agreement financing will be available to us on terms that are acceptable to us. In recent years, investors and financial institutions that lend in the securities repurchase market, have tightened lending standards in response to the difficulties and changed economic conditions that have materially adversely affected the MBS market. These market disruptions have been most pronounced in the Non-Agency MBS market, and the impact has also extended to Agency MBS, which has made the value of these assets unstable and relatively illiquid compared to prior periods. Any decline in their value, or perceived market uncertainty about their value, would make it more difficult for us to obtain financing on favorable terms or at all, or maintain our compliance with terms of any financing arrangements then in place. Additionally, the lenders from which we seek to obtain repurchase agreement financing may have owned or financed MBS that have declined in value and caused the lender to suffer losses as a result of the 2007 to 2010 downturn in the residential, as well as commercial, mortgage markets. If these conditions persist, these institutions may be forced to exit the repurchase market, become insolvent or further tighten lending standards or increase the amount of equity capital or haircut required to obtain financing, and in such event, could make it more difficult for us to obtain financing on favorable terms or at all. Further, the implementation of Basel III and the Dodd Frank Act will increase the regulatory capital which financial institutions must hold against repurchase financing, thereby making the cost of providing such financing more expensive. This is likely to result in less availability of repurchase financing and/or higher pricing. In the event that we cannot obtain sufficient funding on acceptable terms, there may be a negative impact on the value of our common stock and our ability to make distributions, and you may lose part or all of your investment.

As of December 31, 2014, we had amounts outstanding under repurchase agreements with 21 separate lenders, had repurchase agreements with 24 different lenders and our currently in discussions with several additional potential lenders. Prior to entering into a lending relationship with any financial institution, our Manager does a thorough credit review of such potential lender. Notwithstanding the foregoing, a material adverse development involving one or more major financial institutions or the financial markets in general, in addition to the regulatory changes discussed above, could result in our lenders reducing our access to funds available under our repurchase agreements or terminating such agreements altogether. Dramatic declines in the housing market from 2007 to 2010, with decreasing home prices and increasing foreclosures and unemployment, resulted in significant asset write-downs by financial institutions, which caused many financial institutions to seek additional capital, to merge with other institutions, and, in some cases, to fail. As all of our repurchase agreements are uncommitted and renewable at the discretion of our lenders, these conditions could cause our lenders to determine to reduce or terminate our access to future borrowings at virtually any time which could materially adversely affect our business and profitability. Furthermore, if a number of our lenders became unwilling or unable continue to provide us with financing; we could be forced to sell assets in order to maintain liquidity. Forced sales under adverse market conditions may result in lower sales prices than ordinary market sales made in the normal course of business.

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Furthermore, because we rely primarily on short-term borrowings, our ability to achieve our investment objective will depend not only on our ability to borrow money in sufficient amounts and on favorable terms, but also on our ability to renew or replace on a continuous basis our maturing short-term borrowings. If we are not able to renew or replace maturing borrowings due to changes in the regulatory environment or for any other reason, we will have to sell some or all of our assets, possibly under adverse market conditions which may have a material adverse effect on our financial position, results of operations and cash flows. In addition, the aforementioned changes to the regulatory capital requirements imposed on our lenders may significantly increase the cost of the financing that they provide to us. Our lenders also may revise their eligibility requirements for the types of assets they are willing to finance or the terms of such financings, based on, among other factors, the recent changes in the regulatory environment and their management of perceived risk, particularly with respect to assignee liability.

Our repurchase agreement financing may require us to provide additional collateral and may restrict us from leveraging our assets as fully as desired.

We use repurchase agreements to finance acquisitions of our Target Assets. If the market value of the asset pledged or sold by us to a financing institution pursuant to a repurchase agreement declines, we may be required by the financing institution to provide additional collateral or pay down a portion of the funds advanced, but we may not have the funds available to do so, which could result in defaults. Posting additional collateral to support our credit will reduce our liquidity and limit our ability to leverage our assets, which could adversely affect our business. In the event we do not have sufficient liquidity to meet such requirements, financing institutions can accelerate repayment of our indebtedness, increase interest rates, liquidate our collateral or terminate our ability to borrow. Such a situation would likely result in a rapid deterioration of our financial condition and possibly necessitate a filing for bankruptcy protection.

On the date each month that principal payments are announced (i.e., the factor day for our Agency RMBS), the value of our Agency RMBS pledged as collateral under our repurchase agreements is reduced by the amount of the prepaid principal and, as a result, our lenders will typically initiate a margin call requiring the pledge of additional collateral or cash, in an amount equal to such prepaid principal, in order to re-establish the required ratio of borrowing to collateral value under such repurchase agreements. Accordingly, with respect to our Agency RMBS the announcement on factor day of principal prepayments is in advance of our receipt of the related scheduled payment, thereby creating a short-term receivable for us in the amount of such principal prepayments; however, under our repurchase agreements, we may receive a margin call relating to the related reduction in value of our Agency RMBS and prior to receipt of this short-term receivable, be required to post additional collateral or cash in an amount equal to the product of the advance rate of such repurchase agreement and the principal prepayment on or about factor day, which would reduce our liquidity during the period in which the short term receivable is outstanding. As a result, in order to meet any such margin calls, we could be forced to sell assets in order to maintain liquidity. Forced sales under adverse market conditions may result in lower sales prices than ordinary market sales in the normal course of business.

Further, financial institutions providing the repurchase facilities may require us to maintain a certain amount of cash uninvested or to set aside non-levered assets sufficient to maintain a specified liquidity position which would allow us to satisfy our collateral obligations. As a result, we may not be able to leverage our assets as fully as we would choose which could reduce our return on equity. If we are unable to meet these collateral obligations, our financial condition could deteriorate rapidly.

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Lenders may require us to enter into restrictive covenants relating to our operations.

When we obtain further financing, lenders could impose restrictions on us that would affect our ability to incur additional debt, our capability to make distributions to stockholders and our flexibility to determine our operating policies. Loan documents we execute may contain negative covenants that limit, among other things, our ability to repurchase stock, distribute more than a certain amount of our funds from operations, and employ leverage beyond certain amounts.

Our rights under repurchase agreements may be subject to the effects of the bankruptcy laws in the event of the bankruptcy or insolvency of us or our counterparties under the repurchase agreements.

In the event of our insolvency or bankruptcy, certain repurchase agreements may qualify for special treatment under the U.S. Bankruptcy Code, the effect of which, among other things, would be to allow the lender under the applicable repurchase agreement to avoid the automatic stay provisions of the U.S. Bankruptcy Code and to take possession of and liquidate the assets that we have pledged under their repurchase agreements. In the event of the insolvency or bankruptcy of a lender during the term of a repurchase agreement, the lender may be permitted, under applicable insolvency laws, to repudiate the contract, and our claim against the lender for damages may be treated simply as the claim of an unsecured creditor. In addition, if the lender is a broker or dealer subject to the Securities Investor Protection Act of 1970, or an insured depository institution subject to the Federal Deposit Insurance Act, our ability to exercise our rights to recover our securities under a repurchase agreement or to be compensated for any damages resulting from the lender's insolvency may be further limited by those statutes. These claims would be subject to significant delay and, if and when received, may be substantially less than the damages we actually incur.

An increase in our borrowing costs relative to the interest that we receive on our portfolio investments may adversely affect our profitability and cash available for distribution to our stockholders.

As long as we earn a positive spread between interest and other income we earn on our leveraged assets and our borrowing costs, we believe that we can generally increase our profitability by using greater amounts of leverage. We cannot, however, assure you that repurchase financing will remain an efficient source of long-term financing for our assets. The amount leverage that we use may be limited because our lenders might not make funding available to us or they may require that we provide additional collateral to secure our borrowings. If our financing strategy is not viable, we will have to find alternative forms of financing for our assets which may not be available to us on acceptable terms or at acceptable rates. In addition, in response to certain interest rate and investment environments or to changes in the market liquidity, we could adopt a strategy of reducing our leverage by selling assets or not reinvesting principal payments as MBS amortize and/or prepay, thereby decreasing the outstanding amount of our related borrowings. Such an action could reduce interest income, interest expense and net income, the extent of which would be dependent on the level of reduction in assets and liabilities as well as the sale prices for which assets were sold.

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As our financings mature, we will be required either to enter into new borrowings or to sell certain of our investments. Since we rely primarily on borrowings under repurchase agreements to finance our assets, our ability to achieve our investment objectives depends on our ability to borrow funds in sufficient amounts and on acceptable terms, and on our ability to renew or replace maturing borrowings on a continuous basis. Our repurchase agreement credit lines are renewable at the discretion of our lenders and, as such; do not contain guaranteed roll-over terms. Our ability to enter into repurchase transactions in the future will depend on the market value of our assets pledged to secure the specific borrowings, the availability of acceptable financing and market liquidity and other conditions existing in the lending market at that time. If we are unable to renew or replace maturing borrowings, we could be forced to sell assets in order to maintain liquidity. Forced sales under adverse market conditions could result in lower sales prices than ordinary market sales in the normal course of business. Further, an increase in short-term interest rates at the time that we seek to enter into new borrowings would reduce the spread between our returns on our assets and the cost of our borrowings. This would adversely affect our returns on our assets, which might reduce earnings and, in turn, cash available for distribution to our stockholders.

We may enter into hedging transactions that could expose us to contingent liabilities in the future.

Subject to maintaining our qualification as a REIT and exemption from registration under the 1940 Act, part of our investment strategy may involve entering into economic hedging transactions that could require us to fund cash payments in certain circumstances (such as the early termination of the hedging instrument caused by an event of default or other early termination event, or the decision by a counterparty to request margin securities it is contractually owed under the terms of the hedging instrument). The amount due would be equal to the unrealized loss of the open swap positions with the respective counterparty and could also include other fees and charges. These economic losses will be reflected in our results of operations, and our ability to fund these obligations will depend on the liquidity of our assets and access to capital at the time, and the need to fund these obligations could adversely impact our financial condition.

Hedging against interest rate exposure may adversely affect our earnings, which could reduce our cash available for distribution to our stockholders.

Subject to maintaining our qualification as a REIT and exemption from registration under the 1940 Act, we generally pursue various economic hedging strategies to seek to reduce our exposure to adverse changes in interest rates. Our hedging activity varies in scope based on the level and volatility of interest rates, the type of assets held and other changing market conditions. Interest rate hedging may fail to protect or could adversely affect us because, among other things:

- interest rate hedging can be expensive, particularly during periods of rising and volatile interest rates;
- available interest rate hedges may not correspond directly with the interest rate risk for which protection is sought;
- due to a credit loss, the duration of the hedge may not match the duration of the related liability;
- the amount of income that a REIT may earn from hedging transactions (other than hedging transactions that satisfy certain requirements of the Code or that are done through a TRS) to offset interest rate losses is limited by U.S. federal tax provisions governing REITs;
- the value of derivatives used for hedging may be adjusted from time to time in accordance with accounting rules to reflect changes in fair value. Downward adjustments or "mark-to-market losses," would reduce our stockholders' equity;
- the credit quality of the hedging counterparty owing money on the hedge may be downgraded to such an extent that it impairs our ability to sell or assign our side of the hedging transaction; and

the hedging counterparty owing money in the hedging transaction may default on its obligation to pay.

Our hedging transactions, which are intended to limit losses, may actually adversely affect our earnings, which could reduce our cash available for distribution to our stockholders.

While the majority of our interest rate swaps are traded on a regulated exchange, certain hedging instruments are traded over the counter and do not trade on regulated exchanges and, therefore, are not guaranteed by an exchange or a clearing house. In addition over the counter instruments are more lightly regulated by U.S. and foreign governmental authorities. Consequently, there may be no requirements with respect to record keeping, financial responsibility or segregation of customer funds and positions. Furthermore, the enforceability of agreements underlying hedging transactions may depend on compliance with applicable statutory and commodity and other regulatory requirements and, depending on the identity of the counterparty, applicable international requirements. The business failure of a hedging counterparty with whom we enter into a hedging transaction which did not clear through a clearing house would most likely result in its default. Default by a party with whom we enter into a hedging transaction may result in the loss of unrealized profits and force us to cover our commitments, if any, at the then current market price. Although generally we seek to reserve the right to terminate our hedging positions, it may not always be possible to dispose of or close out a hedging position without the consent of the hedging counterparty and we may not be able to enter into an offsetting contract in order to cover our risk. There can be no assurance that a liquid secondary market will exist for any hedging instruments purchased or sold, and we may be required to maintain a position until exercise or expiration, which could result in losses.

Risks associated with our relationship with our Manager

Our Manager has limited experience operating a REIT and we cannot assure you that our Manager's past experience will be sufficient to successfully manage our business as a REIT.

Our Manager has limited experience operating a REIT. The REIT provisions of the Code are complex, and any failure to comply with those provisions in a timely manner could prevent us from qualifying as a REIT or force us to pay unexpected taxes and penalties. In such event, our net income would be reduced and we could incur a loss.

Our Board of Directors has approved very broad investment guidelines for our Manager and does not approve each investment and financing decision made by our Manager.

Our Manager is authorized to follow very broad investment guidelines. Our Board of Directors periodically reviews our investment guidelines and our investment portfolio but does not, and is not required to review all of our proposed investments, except that an investment in a security structured or issued by another entity managed by our Manager must be approved by at least two thirds ($^2/_3$) of our independent directors prior to such investment. In addition, in conducting periodic reviews, our Board of Directors may rely primarily on information provided to them by our Manager. Furthermore, our Manager may use complex strategies, and transactions entered into by our Manager may be costly, difficult or impossible to unwind by the time they are reviewed by our Board of Directors. Our Manager has great latitude within the broad parameters of our investment guidelines in determining the types and amounts of Agency and Non-Agency RMBS, CMBS, ABS and other portfolio investments it may decide are attractive investments for us, which could result in investment returns that are substantially below expectations or that result in losses, which would materially and adversely affect our business operations and results. Further, decisions made and investments and financing arrangements entered into by our Manager may not fully reflect the best interests of our stockholders.

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There are conflicts of interest in our relationship with our Manager that could result in decisions that are not in the best interests of our stockholders.

We are subject to conflicts of interest arising out of our relationship with our Manager. During 2013, all of our officers apart from our chief financial officer, Steven M. Sherwyn, were employees of our Manager. Effective January 1, 2014, Mr. Sherwyn is no longer an employee of the Company, but an employee of our Manager as well. In addition, two of our directors, James W. Hirschmann III and Gavin L. James, are also employees of our Manager. Accordingly, as of January 1, 2014, we do not have any employees. Our Management Agreement with our Manager was negotiated between related parties and its terms, including fees and other amounts payable, may not be as favorable to us as if it had been negotiated at arm's length with an unaffiliated third party. In addition, the obligations of our Manager and its officers and personnel to engage in other business activities may reduce the time our Manager and its officers and personnel spend managing us.

We compete for investment opportunities directly with other client portfolios managed by our Manager. Clients of our Manager may have investment mandates and objectives that target the same assets as us. A substantial number of client accounts managed by our Manager have exposure to RMBS, CMBS and our other portfolio investments and may have similar investment mandates and objectives. In addition, our Manager may have additional clients that compete directly with us for investment opportunities in the future. Our Manager has an investment allocation policy in place that is intended to ensure that no single client is intentionally favored over another and that trades are allocated in a fair and equitable manner. We may compete with our Manager or its other clients for investment or financing opportunities sourced by our Manager; however, we may either not be presented with the opportunity or have to compete with our Manager to acquire these investments or have access to these sources of financing. Our Manager and our executive officers may choose to allocate favorable investments to itself or to its or other clients instead of to us. Further, at times when there are turbulent conditions in the mortgage markets or distress in the credit markets or other times when we will need focused support and assistance from our Manager, our Manager's other clients will likewise require greater focus and attention, placing our Manager's resources in high demand. In such situations, we may not receive the level of support and assistance that we may receive if we were internally managed or if our Manager did not act as a manager for other entities. There is no assurance that our Manager's allocation policies that address some of the conflicts relating to our access to investment and financing sources will be adequate to address all of the conflicts that may arise.

We pay our Manager a management fee that is not tied to our performance. The management fee may not sufficiently incentivize our Manager to generate attractive risk-adjusted returns for us. This could hurt both our ability to make distributions to our stockholders and the market price of our common stock. Furthermore, the compensation payable to our Manager will increase as a result of future issuances of our equity securities, even if the issuances are dilutive to existing stockholders.

Concurrently with our IPO, we sold 46,043 shares of our common stock to our Manager's deferred compensation plan, which made such investment on behalf of the beneficiaries of the plan, including certain executives and other employees of our Manager and its affiliates. These shares are subject to a two-year lock-up agreement from the date of our IPO with the underwriters from that offering. We issued 4,467 shares of our common stock to our Manager's deferred compensation plan on January 28, 2014, as a result of the stock component of our dividend declared on December 19, 2013. In April 2014, in conjunction with a follow-on equity offering, we sold 650,000 shares of common stock to our Manager in a private placement. These shares are subject to two-month lock-up agreement from the date of issuance with the underwriters of our follow-on offering. In addition, through December 31, 2014 our Manager had received three grants of restricted stock totaling 419,023 shares (inclusive of the stock component of the December 19, 2013 dividend). Each grant vests pro-rata over a three year period and to date a total of 90,612 shares have vested. To date, our Manager has not sold any of our common stock. To the extent our Manager elects to sell all or a portion of these shares in the future, our Manager's interests may be less aligned with our interests.

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We are dependent on our Manager and its key personnel for our success.

We have no separate facilities and are completely reliant on our Manager. As of January 1, 2014, all of our executive officers and two of our directors are employees of our Manager. Our Manager has significant discretion as to the implementation of our investment and operating policies and strategies. Accordingly, we believe that our success will depend to a significant extent upon the efforts, experience, diligence, skill and network of business contacts of the executive officers and key personnel of our Manager. The executive officers and key personnel of our Manager evaluate, negotiate, close and monitor our investments; therefore, our success depends on their continued service. The departure of any of the executive officers or key personnel of our Manager could have a material adverse effect on our performance. In addition, we offer no assurance that our Manager will remain our investment manager or that we will continue to have access to our Manager's principals and professionals. The term of our Management Agreement with our Manager has now been extended until May 15, 2016, with automatic one-year renewals thereafter. If the Management Agreement is terminated and no suitable replacement is found to manage us, we may not be able to execute our business plan. Moreover, our Manager is not obligated to dedicate any of its personnel exclusively to us nor is it obligated to dedicate any specific portion of its time to our business, and none of our Manager's personnel are contractually dedicated to us under our Management Agreement with our Manager.

The Management Agreement with our Manager was not negotiated on an arm's-length basis, may not be as favorable to us as if it had been negotiated with an unaffiliated third party and may be costly and difficult to terminate.

As of January 1, 2014, all of our executive officers and two of our directors are employees of our Manager. Our Management Agreement with our Manager was negotiated between related parties and its terms, including fees payable, may not be as favorable to us as if it had been negotiated with an unaffiliated third party.

Termination of the Management Agreement with our Manager without cause is difficult and costly. Our independent directors review our Manager's performance and any fees payable to our Manager annually and, following the initial three-year term, the Management Agreement may be terminated annually upon the affirmative vote of at least two thirds ($^2/_3$) of our independent directors based upon: (i) our Manager's unsatisfactory performance that is materially detrimental to us; or (ii) our determination that any fees payable to our Manager are not fair, subject to our Manager's right to prevent termination based on unfair fees by accepting a reduction of management fees agreed to by at least two thirds ($^2/_3$) of our independent directors. We are required to provide our Manager 180 days prior notice of any such termination. Unless terminated for cause, we are required to pay our Manager a termination fee equal to three times the average annual management fee earned by our Manager during the prior 24-month period immediately preceding such termination, calculated as of the end of the most recently completed fiscal quarter before the date of termination. This provision increases the effective cost to us of electing not to renew, or defaulting in our obligations under, the Management Agreement, thereby adversely affecting our inclination to end our relationship with our Manager, even if we believe our Manager's performance is not satisfactory.

Our Manager is only contractually committed to serve us until May 15, 2016. The Management Agreement is automatically renewable for one-year terms; provided, however, that our Manager may terminate the Management Agreement annually upon 180 days prior notice. If the Management Agreement is terminated and no suitable replacement is found to manage us, we may not be able to execute our business plan.

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Pursuant to the Management Agreement, our Manager does not assume any responsibility other than to render the services called for thereunder and is not responsible for any action of our Board of Directors in following or declining to follow its advice or recommendations. Our Manager maintains a contractual as opposed to a fiduciary relationship with us. Under the terms of the Management Agreement, our Manager, its officers, stockholders, members, managers, directors, personnel, any person controlling or controlled by our Manager and any person providing sub-advisory services to our Manager are not liable to us, our directors, our stockholders or any partners for acts or omissions performed in accordance with and pursuant to the Management Agreement, except because of acts constituting bad faith, willful misconduct, gross negligence, or reckless disregard of their duties under the Management Agreement. In addition, we indemnify our Manager, its officers, stockholders, members, managers, directors, personnel, any person controlling or controlled by our Manager and any person providing sub-advisory services to our Manager with respect to all expenses, losses, damages, liabilities, demands, charges and claims arising from acts of our Manager not constituting bad faith, willful misconduct, gross negligence, or reckless disregard of duties, performed in good faith in accordance with and pursuant to the Management Agreement.

Our Manager's management fee is payable regardless of our performance.

We pay our Manager a management fee regardless of the performance of our portfolio. Our Manager's entitlement to non-performance-based compensation might reduce its incentive to devote its time and effort to seeking assets that provide attractive risk-adjusted returns for our portfolio. This in turn could hurt both our ability to make distributions to our stockholders and the market price of our common stock.

Our Manager is subject to extensive regulation as an investment advisor, which could adversely affect its ability to manage our business.

Our Manager is subject to regulation as an investment advisor by various regulatory authorities that are charged with protecting the interests of its clients, including us. Instances of criminal activity and fraud by participants in the investment management industry and disclosures of trading and other abuses by participants in the financial services industry have led the U.S. government and regulators to consider increasing the rules and regulations governing, and oversight of, the U.S. financial system. This activity is expected to result in changes to the laws and regulations governing the investment management industry and more aggressive enforcement of the existing laws and regulations. Our Manager could be subject to civil liability, criminal liability, or sanction, including revocation of its registration as an investment adviser, revocation of the licenses of its employees, censures, fines, or temporary suspension or permanent bar from conducting business, if it is found to have violated any of these laws or regulations. Any such liability or sanction could adversely affect its ability to manage our business. Our Manager must continually address conflicts between its interests and those of its clients, including us. In addition, the SEC and other regulators have increased their scrutiny of potential conflicts of interest. We believe our Manager has procedures and controls that are reasonably designed to address these issues. However, appropriately dealing with conflicts of interest is complex and difficult and if our Manager fails, or appears to fail, to deal appropriately with conflicts of interest, it could face litigation or regulatory proceedings or penalties, any of which could adversely affect its ability to manage our business.

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In fact, in January 2014 settlements of two separate and unrelated regulatory matters involving our Manager with the United States Department of Labor and the Securities and Exchange Commission were announced. The first matter involved the trading of Non-Agency RMBS and whether certain trades complied with the cross trading rules applicable to pension plans subject to Employee Retirement Income Security Act ("ERISA") and to SEC registered funds under the 1940 Act. Our Manager settled that matter without admitting or denying the charges and paying approximately $7.4 million in compensation to clients and approximately $1.6 million in fines to the regulators. The second matter involved the handling of an investment which prohibited ERISA accounts from holding it which was allocated in error to certain ERISA accounts. Our Manager settled that matter without admitting or denying the charges and paying $10 million in compensation and $2 million in fines. Neither matter related to the Company. The settlements will not adversely affect our Manager's ability to manage the Company's affairs.

Risks related to our common stock

The market price and trading volume of our common stock may vary substantially.

Our common stock is listed on the NYSE under the symbol "WMC". The stock markets, including the NYSE, have experienced significant price and volume fluctuations over the past several years. As a result, the market price of our common stock is likely to be similarly volatile, and investors in our common stock may experience a decrease in the value of their shares. Accordingly, no assurance can be given as to the ability of our stockholders to sell their common stock or the price that our stockholders may obtain for their common stock.

Some of the factors that could negatively affect the market price of our common stock include:

- actual or anticipated variations in our quarterly operating results;
- changes in our earnings estimates or publication of research reports about us or the real estate industry;
- changes in market valuations of similar companies;
- adverse market reaction to any increased indebtedness we incur in the future;
- additions to or departures of our Manager's key personnel;
- actions by our stockholders; and
- speculation in the press or investment community.

Market factors unrelated to our performance could also negatively impact the market price of our common stock. One of the factors that investors may consider in deciding whether to buy or sell our common stock is our distribution rate as a percentage of our stock price relative to market interest rates. If market interest rates increase, prospective investors may seek alternative investments paying higher dividends or interest. As a result, interest rate fluctuations and conditions in the capital markets can affect the market value of our common stock. For instance, if interest rates rise, it is likely that the market price of our common stock will decrease as market rates on interest-bearing securities increase.

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For as long as we are an emerging growth company, we will not be required to comply with certain reporting requirements, including those relating to accounting standards and disclosure about our executive compensation, that apply to other public companies.

In April 2012, President Obama signed into law the Jumpstart Our Business Startups Act, or the JOBS Act. The JOBS Act contains provisions that, among other things, relax certain reporting requirements for "emerging growth companies," including certain requirements relating to accounting standards and compensation disclosure. We are classified as an emerging growth company. For as long as we are an emerging growth company, which may be up to five full fiscal years from the date of our IPO, unlike other public companies, we will not be required to: (i) provide an auditor's attestation report on management's assessment of the effectiveness of our system of internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act; (ii) comply with any new or revised financial accounting standards applicable to public companies until such standards are also applicable to private companies under Section 102(b)(1) of the JOBS Act; (iii) comply with any new requirements adopted by the Public Company Accounting Oversight Board, or the PCAOB, requiring mandatory audit firm rotation or a supplement to the auditor's report in which the auditor would be required to provide additional information about the audit and the financial statements of the issuer; (iv) comply with any new audit rules adopted by the PCAOB after April 5, 2012 unless the SEC determines otherwise; (v) provide certain disclosure regarding executive compensation required of larger public companies; or (vi) hold shareholder advisory votes on executive compensation. We cannot predict if investors will find our common stock less attractive if we choose to rely on these exemptions. If some investors find our common stock less attractive as a result of any choices to reduce future disclosure, there may be a less active trading market for our common stock and our stock price may be more volatile.

As noted above, under the JOBS Act, emerging growth companies can delay adopting new or revised accounting standards that have different effective dates for public and private companies until such time as those standards apply to private companies. We currently take advantage of such extended transition period. Since we are not required to comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for other public companies, our financial statements may not be comparable to the financial statements of companies that comply with public company effective dates. If we were to elect to comply with these public company effective dates, such election would be irrevocable pursuant to Section 107 of the JOBS Act.

Investing in our common stock may involve a high degree of risk.

The investments that we make in accordance with our investment objectives may result in a high amount of risk when compared to alternative investment options and volatility or loss of principal. Our investments may be highly speculative and aggressive, and therefore an investment in our common stock may not be suitable for someone with lower risk tolerance.

Common stock eligible for future sale may have adverse effects on our share price.

We cannot predict the effect, if any, of future sales of our common stock, or the availability of shares for future sales, on the market price of our common stock. The market price of our common stock may decline significantly when the restrictions on resale (or lock up agreements) by certain of our stockholders lapse. Sales of substantial amounts of common stock or the perception that such sales could occur may adversely affect the prevailing market price for our common stock.

Also, we may issue additional shares in follow-on public offerings or private placements to make new investments or for other purposes. We are not required to offer any such shares to existing stockholders on a preemptive basis. Therefore, it may not be possible for existing stockholders to participate in such future share issuances, which may dilute the existing stockholders' interests in us.

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We have not established a minimum distribution payment level and we cannot assure you of our ability to pay distributions in the future.

We intend to pay quarterly distributions and to make distributions to our stockholders in an amount such that we distribute all or substantially all of our net taxable income, calculated in accordance with the REIT regulations, each year. We have not established a minimum distribution payment level and our ability to pay distributions may be adversely affected by a number of factors, including the risk factors described herein. All distributions will be made at the discretion of our Board of Directors and will depend on our earnings, our financial condition, debt covenants, maintenance of our REIT qualification and other factors as our Board of Directors may deem relevant from time to time. We believe that a change in any one of the following factors could adversely affect our results of operations and impair our ability to pay distributions to our stockholders:

- the profitability of our existing investments and the investment of net proceeds of any subsequent offering;
- our ability to make profitable investments;
- margin calls or other expenses that reduce our cash flow;
- decreases in the value of our portfolio or defaults in our asset portfolio; and
- the fact that anticipated operating expense levels may not prove accurate, as actual results may vary from estimates.

We cannot assure you that we will achieve investment results that will allow us to make a specified level of cash distributions or year-to-year increases in cash distributions in the future. In addition, some of our distributions may include a return in capital.

Future offerings of debt or equity securities, which would rank senior to our common stock, may adversely affect the market price of our common stock.

If we decide to issue debt or equity securities in the future, which would rank senior to our common stock, it is likely that they will be governed by an indenture or other instrument containing covenants restricting our operating flexibility. Additionally, any convertible or exchangeable securities that we issue in the future may have rights, preferences and privileges more favorable than those of our common stock and may result in dilution to owners of our common stock. We and, indirectly, our stockholders, will bear the cost of issuing and servicing such securities. Because our decision to issue debt or equity securities in any future offering will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of our future offerings. Thus holders of our common stock will bear the risk of our future offerings reducing the market price of our common stock and diluting the value of their stock holdings in us. Furthermore, the compensation payable to our Manager will increase as a result of future issuances of our equity securities, including issuances upon exercise of the warrants, described below, even if the issuances are dilutive to existing stockholders.

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The dilutive effect of our outstanding warrants, including in certain circumstances, upon the future issuance of common stock, could have an adverse effect on the future market price of our common stock or otherwise adversely affect the interests of our common stockholders.

On May 15, 2012, we issued and sold to certain institutional investors a number of warrants entitling them to purchase up to an aggregate of 1,115,893 shares of our common stock. These warrants had an initial exercise price of $20.50 per share (subject to adjustment and limitation on exercise in certain circumstances) and are exercisable for seven years after the date of the warrants' issuance, or earlier upon notice of redemption by us. On October 3, 2012, the exercise price was adjusted to 19.44, as a result of the follow-on public offering. In addition, on January 28, 2014 the exercise price was further reduced to $17.59, as a result of the stock portion of our dividend declared on December 19, 2013 and the number of shares purchasable increased to 1,232,916. As a result of the April 3, 2014 follow-on public offering and private placement, the exercise price of each of the outstanding warrants was reduced from $17.59 to $16.70. The exercise of the warrants in the future would be dilutive to holders of our common stock if our book value per share or the market price of our common stock is higher than the exercise price at the time of exercise. The potential for dilution from the warrants could have an adverse effect on the future market price of our common stock.

Further, the exercise price of the warrants will be adjusted under certain circumstances, including, subject to certain exceptions, if we sell common stock (or other securities convertible into or exchangeable for our common stock) in a public offering or private placement, for cash at a price per share (after deduction of underwriting discounts or placement fees and other expenses incurred by us that are attributable to the offering) that is less than the closing price of our common stock immediately prior to: (i) the announcement of the proposed sale in the case of public offerings; or (ii) the execution of the purchase agreement in the case of private placements. Accordingly, the exercise price will be adjusted downward in connection with any future offering and increase the dilutive effect of the warrants. Furthermore, any similar public offerings or private placements of our common stock we conduct in the future will likely increase the dilutive effect of the warrants.

Risks related to our organization and structure

Our authorized but unissued shares of common and preferred stock may prevent a change in our control.

Our amended and restated certificate of incorporation authorizes us to issue additional authorized but unissued shares of common or preferred stock. In addition, our Board of Directors may, without stockholder approval, amend our amended and restated certificate of incorporation to increase the aggregate number of our shares of stock or the number of shares of stock of any class or series that we have authority to issue and classify or reclassify any unissued shares of common or preferred stock and set the preferences, rights and other terms of the classified or reclassified shares. As a result, our Board of Directors may establish a series of shares of common or preferred stock that could delay or prevent a transaction or a change in control that might involve a premium price for our shares of common stock or otherwise be in the best interest of our stockholders.

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Ownership limitations may restrict change of control or business combination opportunities in which our stockholders might receive a premium for their shares.

In order for us to qualify as a REIT for each taxable year after 2012, no more than 50% in value of our outstanding capital stock may be owned, directly or indirectly, by five or fewer individuals during the last half of any calendar year. "Individuals" for this purpose include natural persons, private foundations, some employee benefit plans and trusts, and some charitable trusts. To assist us in maintaining our qualification as a REIT, our amended and restated certificate of incorporation generally prohibits any person from directly or indirectly owning more than 9.8% in value or in number of shares, whichever is more restrictive, of the outstanding shares of our capital stock or more than 9.8% in value or in number of shares, whichever is more restrictive, of the outstanding shares of our common stock. This ownership limitation could have the effect of discouraging a takeover or other transaction in which holders of our common stock might receive a premium for their shares over the then prevailing market price or which holders might believe to be otherwise in their best interests.

Provisions in our amended and restated certificate of incorporation, our amended and restated bylaws and Delaware law may have the effect of preventing or hindering a change in control and adversely affecting the market price of our common stock.

Provisions in our amended and restated certificate of incorporation and our amended and restated bylaws and applicable provisions of the Delaware General Corporation Law may make it more difficult and expensive for a third party to acquire control of us even if a change of control would be beneficial to the interests of our stockholders. These provisions could discourage potential takeover attempts and could adversely affect the market price our common stock.

We may pay distributions from offering proceeds, borrowings or the sale of assets to the extent that distributions exceed earnings or cash flow from our operations.

We may pay distributions from offering proceeds, borrowings or the sale of assets to the extent that distributions exceed earnings or cash flow from our operations. Such distributions would reduce the amount of cash we have available for investing and other purposes and could be dilutive to our financial results. In addition, funding our distributions from our net proceeds may constitute a return of capital to our investors, which would have the effect of reducing each stockholder's basis in its shares of common stock.

Tax risks

If we do not qualify as a REIT or fail to remain qualified as a REIT, we will be subject to U.S. federal income tax as a regular corporation and could face a substantial tax liability, which would reduce the amount of cash available for distribution to our stockholders.

We believe we have operated and intend to continue to operate in a manner that allows us to qualify as a REIT commencing with our taxable year ended December 31, 2012. Our ability to satisfy the asset tests depends upon our analysis of the characterization and fair market values of our assets, some of which are not susceptible to a precise determination, and for which we will not obtain independent appraisals. Our compliance with the REIT income and quarterly asset requirements also depends upon our ability to successfully manage the composition of our income and assets on an ongoing basis. Accordingly, there can be no assurance that the IRS will not contend that our interests in subsidiaries or in securities of other issuers will not cause a violation of the REIT requirements.

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If we were to fail to qualify as a REIT in any taxable year, we would be subject to U.S. federal income tax, including any applicable alternative minimum tax, on our taxable income at regular corporate rates, and dividends paid to our stockholders would not be deductible by us in computing our taxable income. Any resulting corporate tax liability could be substantial and would reduce the amount of cash available for distribution to our stockholders, which in turn could have an adverse impact on the value of our common stock. Unless we were entitled to relief under certain Code provisions, we also would be disqualified from taxation as a REIT for the four taxable years following the year in which we failed to qualify as a REIT.

Dividends payable by REITs do not qualify for the reduced tax rates available for some dividends.

The maximum tax rate applicable to income from "qualified dividends" payable to U.S. stockholders that are individuals, trusts and estates is currently 20%, exclusive of the 3.8% investment tax surcharge. Dividends payable by REITs, however, generally are not eligible for the qualified dividend reduced rates. Although the rules do not adversely affect the taxation of REITs or dividends payable by REITs, the more favorable rates applicable to regular corporate qualified dividends could cause investors who are individuals, trusts and estates to perceive investments in REITs to be relatively less attractive than investments in the stocks of non-REIT corporations that pay dividends, which could adversely affect the value of the stock of REITs, including our common stock.

REIT distribution requirements could adversely affect our ability to execute our business plan.

We generally must distribute annually at least 90% of our net taxable income, determined without regard to the dividends paid deduction and excluding net capital gains, in order for U.S. federal corporate income tax not to apply to earnings that we distribute. To the extent that we satisfy this distribution requirement, but distribute less than 100% of our REIT taxable income, we will be subject to U.S. federal corporate income tax on our undistributed REIT taxable income. In addition, we will be subject to a 4% nondeductible excise tax if the actual amount that we pay out to our stockholders in a calendar year is less than a minimum amount specified under U.S. federal tax laws. We intend to continue to make distributions to our stockholders to comply with the REIT requirements of the Internal Revenue Code.

From time to time, we may generate taxable income greater than our income for financial reporting purposes prepared in accordance with U.S. GAAP, or differences in timing between the recognition of taxable income and the actual receipt of cash may occur. For example, the tax code limits our ability to use capital losses to offset ordinary income, thereby requiring us to distribute such ordinary income. If we do not have other funds available in these situations we could be required to borrow funds on unfavorable terms, sell investments at disadvantageous prices or distribute amounts that would otherwise be invested in future acquisitions to make distributions sufficient to enable us to pay out enough of our taxable income to satisfy the REIT distribution requirement and to avoid corporate income tax and the 4% excise tax in a particular year. These alternatives could increase our costs or reduce our equity. Thus, compliance with the REIT requirements may hinder our ability to grow, which could adversely affect the value of our common stock.

Even if we remain qualified as a REIT, we may face other tax liabilities that reduce our cash flow.

Even if we remain qualified for taxation as a REIT, we may be subject to certain U.S. federal, state and local taxes on our income and assets, including taxes on any undistributed income, tax on income from some activities conducted as a result of a foreclosure, and state or local income, property and transfer taxes, such as mortgage recording taxes. Any of these taxes would decrease cash available for distribution to our stockholders. In addition, in order to meet the REIT qualification requirements, or to avert the imposition of a 100% tax that applies to certain gains derived by a REIT from dealer property or inventory, we hold some of our assets through a TRS or other subsidiary corporation that will be subject to corporate-level income tax at regular rates. Any of these taxes would decrease cash available for distribution to our stockholders.

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Complying with REIT requirements may cause us to liquidate or forgo otherwise attractive opportunities.

To qualify as a REIT, we must ensure that at the end of each calendar quarter, at least 75% of the value of our assets consists of cash, cash items, government securities and qualified REIT real estate assets, including certain mortgage loans and securities. The remainder of our investments (other than government securities and qualified real estate assets) generally cannot include more than 10% of the outstanding voting securities of any one issuer or more than 10% of the total value of the outstanding securities of any one issuer. In addition, in general, no more than 5% of the value of our total assets (other than government securities and qualified real estate assets) can consist of the securities of any one issuer, and no more than 25% of the value of our total assets can be represented by securities of one or more TRSs. If we fail to comply with these requirements at the end of any calendar quarter, we must correct the failure within 30 days after the end of the calendar quarter or qualify for certain statutory relief provisions to avoid losing our REIT qualification and suffering adverse tax consequences. As a result, we may be required to liquidate from our investment portfolio otherwise attractive investments. These actions could have the effect of reducing our income and amounts available for distribution to our stockholders.

In addition to the asset tests set forth above, to qualify as a REIT we must continually satisfy tests concerning, among other things, the sources of our income, the amounts we distribute to our stockholders and the ownership of our stock. We may be unable to pursue investments that would be otherwise advantageous to us in order to satisfy the source-of-income or asset- diversification requirements for qualifying as a REIT. Thus, compliance with the REIT requirements may hinder our ability to make certain attractive investments.

We may be required to report taxable income for certain investments in excess of the economic income we ultimately realize from them.

We acquired and may acquire in the future mortgage-backed securities and other portfolio instruments in the secondary market for less than their face amount. In addition, pursuant to our ownership of certain mortgage-backed securities, we may be treated as holding certain debt instruments acquired in the secondary market for less than their face amount. The discount at which such securities or debt instruments are acquired may reflect doubts about their ultimate collectability rather than current market interest rates. The amount of such discount will nevertheless generally be treated as "market discount" for U.S. federal income tax purposes. Accrued market discount is reported as income when, and to the extent that, any payment of principal of the mortgage-backed security or debt instrument is made. If we collect less on the mortgage-backed security or debt instrument than our purchase price plus the market discount we had previously reported as income, we may not be able to benefit from any offsetting capital loss deductions to the extent we do not have offsetting capital gains.

In addition, pursuant to our ownership of certain mortgage-backed securities or debt instruments, we may be treated as holding distressed debt investments that are subsequently modified by agreement with the borrower. If the amendments to the outstanding debt are "significant modifications" under applicable Treasury regulations, the modified debt may be considered to have been reissued to us at a gain in a debt-for-debt exchange with the borrower. In that event, we may be required to recognize taxable gain to the extent the principal amount of the modified debt exceeds our adjusted tax basis in the unmodified debt, even if the value of the debt or the payment expectations have not changed.

Moreover, some of the mortgage-backed securities or debt instruments that we acquire may have been issued with original issue discount. We are required to report such original issue discount based on a constant yield method and will be taxed based on the assumption that all future projected payments due on such mortgage-backed securities will be made. If such mortgage-backed securities turn out not to be fully collectable, an offsetting loss deduction will become available only in the later year that uncollectability is provable.

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Finally, in the event that mortgage-backed securities or any debt instruments we are treated as holding pursuant to our investments in mortgage-backed securities are delinquent as to mandatory principal and interest payments, we may nonetheless be required to continue to recognize the unpaid interest as taxable income as it accrues, despite doubt as to its ultimate collectability. Similarly, we may be required to accrue interest income with respect to subordinate mortgage-backed securities at the stated rate regardless of whether corresponding cash payments are received or are ultimately collectable. In each case, while we would in general ultimately have an offsetting loss deduction available to us when such interest was determined to be uncollectable, the utility of that deduction could depend on our having taxable income in that later year or thereafter.

Certain apportionment rules may affect our ability to comply with the REIT asset and gross income tests.

The Code provides that a regular or a residual interest in a real estate mortgage investment conduit, or REMIC, is generally treated as a real estate asset for the purpose of the REIT asset tests, and any amount includible in our gross income with respect to such an interest is generally treated as interest on an obligation secured by a mortgage on real property for the purpose of the REIT gross income tests. If, however, less than 95% of the assets of a REMIC in which we hold an interest consist of real estate assets (determined as if we held such assets), we will be treated as holding our proportionate share of the assets of the REMIC for the purpose of the REIT asset tests and receiving directly our proportionate share of the income of the REMIC for the purpose of determining the amount of income from the REMIC that is treated as interest on an obligation secured by a mortgage on real property. In connection with the expanded Agency RMBS-backed HARP loan program in which we may invest, the IRS issued guidance providing that, among other things, if a REIT holds a regular interest in an "eligible REMIC," or a residual interest in an "eligible REMIC" that informs the REIT that at least 80% of the REMIC's assets constitute real estate assets, then the REIT may treat 80% of the interest in the REMIC as a real estate asset for the purpose of the REIT income and asset tests. Although the portion of the income from such a REMIC interest that does not qualify for purposes of the REIT 75% gross income test would likely be qualifying income for the purpose of the 95% REIT gross income test, the remaining 20% of the REMIC interest generally would not qualify as a real estate asset, which could adversely affect our ability to satisfy the REIT asset tests. Accordingly, owning such a REMIC interest could adversely affect our ability to qualify as a REIT.

The "taxable mortgage pool" rules may increase the taxes that we or our stockholders may incur, and may limit the manner in which we effect future securitizations.

Securitizations could result in the creation of taxable mortgage pools for U.S. federal income tax purposes. As a REIT, so long as we own 100% of the equity interests in a taxable mortgage pool, we generally would not be adversely affected by the characterization of the securitization as a taxable mortgage pool. Certain categories of stockholders, however, such as foreign stockholders eligible for treaty or other benefits, stockholders with net operating losses, and certain tax-exempt stockholders that are subject to unrelated business income tax, could be subject to increased taxes on a portion of their dividend income from us that is attributable to the taxable mortgage pool. In addition, to the extent that our stock is owned by tax-exempt "disqualified organizations," such as certain government-related entities and charitable remainder trusts that are not subject to tax on unrelated business income, we may incur a corporate level tax on a portion of our income from the taxable mortgage pool. In that case, we may reduce the amount of our distributions to any disqualified organization whose stock ownership gave rise to the tax. Moreover, we would be precluded from selling equity interests in these securitizations to outside investors, or selling any debt securities issued in connection with these securitizations that might be considered to be equity interests for tax purposes. These limitations may prevent us from using certain techniques to maximize our returns from securitization transactions.

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Our ability to invest in and dispose of "to be announced" securities could be limited by our election to be subject to tax as a REIT.

We may purchase Agency RMBS through "to-be-announced" forward contracts, or TBAs. In certain instances, rather than take delivery of the Agency RMBS subject to a TBA, we may dispose of the TBA through a dollar roll transaction in which we agree to purchase similar securities in the future at a predetermined price or otherwise, which may result in the recognition of income or gains. We account for dollar roll transactions as purchases and sales of securities. The law is unclear regarding whether TBAs will be qualifying assets for the 75% asset test and whether income and gains from dispositions of TBAs will be qualifying income for the 75% gross income test. Accordingly, our ability to purchase Agency RMBS through TBAs and to dispose of TBAs, through dollar roll transactions or otherwise, could be limited.

The failure of securities subject to repurchase agreements to qualify as real estate assets could adversely affect our ability to qualify as a REIT.

We enter into financing arrangements that are structured as sale and repurchase agreements pursuant to which we nominally sell certain of our securities to a counterparty and simultaneously enter into an agreement to repurchase these securities at a later date in exchange for a purchase price. Economically, these agreements are financings which are secured by the securities sold pursuant thereto. We believe that we will be treated for REIT asset and income test purposes as the owner of the securities that are the subject of any such sale and repurchase agreement notwithstanding that such agreement may transfer record ownership of the securities to the counterparty during the term of the agreement. It is possible, however, that the IRS could assert that we did not own the securities during the term of the sale and repurchase agreement, in which case we could fail to qualify as a REIT.

Liquidation of assets may jeopardize our REIT qualification.

To qualify as a REIT, we must comply with requirements regarding our assets and our sources of income. If we are compelled to liquidate our investments to repay obligations to our lenders, we may be unable to comply with these requirements, ultimately jeopardizing our qualification as a REIT, or we may be subject to a 100% tax on any resultant gain if we sell assets that are treated as dealer property or inventory.

Complying with REIT requirements may limit our ability to hedge effectively and may cause us to incur tax liabilities.

The REIT provisions of the Code substantially limit our ability to hedge our assets and liabilities. Any income from a hedging transaction we enter into to manage risk of interest rate changes with respect to borrowings made or to be made to acquire or carry real estate assets does not constitute "gross income" for purposes of the 75% or 95% gross income tests. To the extent that we enter into other types of hedging transactions, the income from those transactions is likely to be treated as non-qualifying income for purposes of both of the gross income tests. As a result of these rules, we limit our use of advantageous hedging techniques, and we may implement those hedges through a domestic TRS. This could increase the cost of our hedging activities because our TRS would be subject to tax on gains or expose us to greater risks associated with changes in interest rates than we would otherwise want to bear. In addition, losses in our TRS will generally not provide any tax benefit, except for being carried forward against future taxable income in the TRS.

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Qualifying as a REIT involves highly technical and complex provisions of the Code.

Qualification as a REIT involves the application of highly technical and complex Code provisions for which only limited judicial and administrative authorities exist. Even a technical or inadvertent violation could jeopardize our REIT qualification. Our qualification as a REIT will depend on our satisfaction of certain asset, income, organizational, distribution, stockholder ownership and other requirements on a continuing basis. In addition, our ability to satisfy the requirements to qualify as a REIT depends in part on the actions of third parties over which we have no control or only limited influence, including in cases where we own an equity interest in an entity that is classified as a partnership for U.S. federal income tax purposes.

Item 1B. Unresolved Staff Comment

None

Item 2. Properties

We do not own any property. Our executive and administrative offices are located in Pasadena, California in office space shared with our Manager.

Item 3. Legal Proceedings

None.

Item 4. Mine Safety Disclosures.

Not applicable.

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PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock is listed on the NYSE under the symbol "WMC". The following table sets forth the high, low and last sales prices for our common stock, as reported on the NYSE:

Period	High	Low	Close
2014			
First Quarter	$ 17.05	$ 14.64	$ 15.64
Second Quarter	$ 15.68	$ 13.50	$ 14.17
Third Quarter	$ 15.34	$ 13.51	$ 14.78
Fourth Quarter	$ 15.81	$ 13.91	$ 14.70
2013			
First Quarter	$ 23.49	$ 19.90	$ 23.24
Second Quarter	$ 23.98	$ 16.37	$ 17.46
Third Quarter	$ 17.86	$ 14.55	$ 15.99
Fourth Quarter	$ 17.48	$ 14.75	$ 14.88

The following table summarizes our dividends declared on common stock, on a per share basis, for the years ended 2014 and 2013:

Declaration Date	Record Date	Payment Date	Common Stock Dividend
2014			
March 20, 2014	March 31, 2014	April 29, 2014	$ 0.67
June 19, 2014	June 30, 2014	July 29, 2014	$ 0.67
September 23, 2014	October 3, 2014	October 28, 2014	$ 0.70
December 18, 2014	December 29, 2014	January 27, 2015	$ 0.70
2013			
April 1, 2013	April 12, 2013	April 30, 2013	$ 0.95
June 20, 2013	July 1, 2013	July 29, 2013	$ 0.90
September 19, 2013	September 30, 2013	October 29, 2013	$ 0.90
December 19, 2013	December 30, 2013	January 28, 2014	$ 2.35(1)

(1) Consisting of cash and stock. For stockholders who elected to receive the entire $2.35 per share dividend in stock, each stockholder received 0.1590 shares in newly issued common stock for each common share that they held as of the dividend record date. For stockholders who elected to receive the dividend in cash, or did not make an election, each stockholder received $0.9159 per share in cash and 0.0970 shares in newly issued common stock for each common share that they held as of the dividend record date.

In order to maintain our qualification as a REIT, we must make annual distributions to our stockholders of at least 90% of our taxable income (not including net capital gains). We have adopted a policy of paying regular quarterly dividends on our common stock. A combination of cash and stock dividends has been paid on our common stock since our initial public offering. Dividends are declared at the discretion of the Board of Directors and depend on actual and anticipated cash from operations, our financial condition, capital requirements, the annual distribution requirements under the REIT provisions of the Internal Revenue Code and other factors the Board of Directors may consider relevant.

As of March 2, 2015, we had 6 registered holders of our common stock and 41,719,801 shares outstanding.

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Securities Authorized for Issuance Under Equity Compensation Plans

In conjunction with our IPO and concurrent private placement, our Board of Directors approved the Western Asset Mortgage Capital Corporation Equity Plan (the "Equity Plan") and the Western Asset Manager Equity Plan (the "Manager Equity Plan" and collectively the "Equity Incentive Plans"). For further details, see Note 12 to the consolidated financial statements included under Item 8 in this Form 10-K.

The following table presents certain information about the Equity Incentive Plans as of December 31, 2014:

Award	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans
Restricted common stock	N/A	N/A	761,511
Total			761,511

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Stockholder Return Performance

The following graph is a comparison of the cumulative total stockholder return on the Company's common stock, the Standard & Poor's 500 Index (the "S&P 500 Index"), the Russell 2000 Index (the "Russell 2000") and the SNL Finance REIT Index (the "SNL Finance REIT"), a peer group index from May 9, 2012 (commencement of trading on the New York Stock Exchange) to December 31, 2014, and accordingly does not take into account the dividend the Company declared on December 18, 2014 and paid on January 27, 2015. The graph assumes that $100 was invested on May 15, 2012 in the Company's common stock, the S&P 500 Index, the Russell 2000 and the SNL Finance REIT and that all dividends were reinvested without the payment of any commissions. There can be no assurance that the performance of the Company's shares will continue in line with the same or similar trends depicted in the graph below.

Recent Sales of Unregistered Securities: Use of Proceeds from Registered Securities

Not applicable.

Repurchase of Equity Securities

On July 31, 2014, the Board of Directors of the Company approved the repurchase of up to 2,050,000 shares of its common stock through December 31, 2015, either in the open market or through privately-negotiated transactions. The Company made no share repurchases in 2014.

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Item 6. Selected Financial Data

The information below should be read in conjunction with "Forward Looking Statements", Item 1A. "Risk Factors," Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our financial statements and notes thereto included in Item 8. "Financial Statements and Supplementary Data," included in this Form 10-K.

The selected historical information presented for the years ended December 31, 2014, December 31, 2013 and for the period from May 15, 2012 (commencement of operations) through December 31, 2012, relates to our operations and has been derived from our audited Consolidated Statement of Operations included in this Annual Report on Form 10-K.

in thousands except share and per share data	Year Ended December 31, 2014	Year Ended December 31, 2013	For the period from May 15, 2012 (commencement of operations) through December 31, 2012
Operating Data:			
Net Interest Income:			
Interest income	$ 149,110	$ 125,328	$ 53,318
Interest expense	22,263	18,019	8,094
Net Interest Income	126,847	107,309	45,224
Other Income (Loss):			
Interest income on cash balances and other income (loss), net	1,433	91	11
Realized gain (loss) on sale of Mortgage-backed securities and other securities, net	(2,178)	(110,712)	20,754
Other loss on Mortgage-backed securities and other securities, net	(17,014)	(11,858)	(3,206)
Unrealized gain (loss) on Mortgage-backed securities, other securities and whole-loans, net	189,011	(160,109)	13,930
Gain on linked transactions, net	1,870	4,137	
Gain (loss) on derivative instruments, net	(180,496)	157,547	(13,106)
Other Income (Loss), net	(7,374)	(120,904)	18,383
Operating expenses	18,760	14,260	6,330
Net income (loss) available to Common Stock and participating securities	$ 100,713	$ (27,855)	$ 57,277
Net income (loss) per Common Share Basic	$ 2.67	$ (1.19)	$ 3.64
Net income (loss) per Common Share Diluted	$ 2.67	$ (1.19)	$ 3.63
Dividends Declared per Share of Common Stock	$ 2.74	$ 5.10(1)	$ 2.35
Balance Sheet Data (at period end):			
Total assets	$ 4,909,277	$ 3,094,877	$ 5,364,964

Total liabilities	$	4,286,065	$	2,683,783	$	4,841,756
Total stockholders' equity	$	623,212	$	410,094	$	523,208
Other Data:						
Cash flow from (used in):						
Operating activities	$	107,374	$	179,341	$	33,518
Investing activities	$	(1,311,678)	$	2,002,411	$	(5,216,160)
Financing activities	$	1,203,001	$	(2,189,519)	$	5,238,933

(1) Includes $2.35 dividend per share declared on December 19, 2013, consisting of cash and stock.

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ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion should be read in conjunction with our financial statements and accompanying notes included in Item 8, "Financial Statements and Supplementary Data" of this annual report on Form 10-K.

Overview

We are organized as a Delaware corporation. We operate and elected to be taxed as a REIT, commencing with our taxable year ended December 31, 2012. We generally will not be subject to U.S. federal income taxes on our taxable income to the extent that we annually, in accordance with the REIT regulations, distribute all of our net taxable income to stockholders and maintain our intended qualification as a REIT. We also intend to operate our business in a manner that will permit us to maintain our exemption from registration under the 1940 Act.

Our consolidated financial statements include our accounts, those of our wholly owned taxable REIT subsidiary or "TRS" and a trust that meets the definition of a variable interest entity ("VIE") related to the acquisition of residential whole-loans in which we are the primary beneficiary. The trust has issued trust certificates to us which are collateralized by pools of residential mortgage loans held by the trust. We include the underlying residential whole-loans owned by the trust in Residential whole-loans at fair value on our Consolidated Balance Sheets and have eliminated the trust certificates in consolidation.

We are externally managed and advised by our Manager, an SEC-registered investment advisor and a wholly-owned subsidiary of Legg Mason, Inc. Our Manager is responsible for administering our business activities and our day-to-day operations, subject to the supervision of our Board of Directors.

On April 3, 2014, we entered into a binding agreement with a group of underwriters to sell an incremental 13.0 million shares of our common stock, which closed on April 9, 2014. The agreement provided the underwriters with the right to purchase an additional 1.95 million shares (15% of 13.0 million) during the succeeding thirty (30) days. The shares were offered to the market at a price of $14.85 per share and the underwriters exercised a portion of their option and purchased an incremental 1.0 million shares on May 2, 2014, which closed on May 7, 2014. We received net proceeds of approximately $205.4 million after subtracting underwriting commissions and offering expenses of approximately $2.9 million. On April 3, 2014, we also entered into an agreement to sell 650,000 shares of our common stock, for $14.85 per share, to our Manager in a private placement for an aggregate offering price of approximately $9.7 million, which closed on April 9, 2014.

We have invested the proceeds of our IPO, concurrent private placements and follow-on public offerings in Agency RMBS, including Mortgage pass-through certificates, Agency derivatives, Agency Interest-Only Strips, and Agency CMOs, Non-Agency RMBS as well as Agency and Non-Agency CMBS, Non U.S. CMBS, ABS and residential whole-loans. We have also used "to-be-announced" forward contracts, or TBAs, in order to invest in Agency RMBS. Pursuant to these TBAs, we agree to purchase (or deliver), for future settlement, Agency RMBS with certain principal and interest terms. At December 31, 2014, our portfolio was comprised of approximately $3.2 billion of Agency RMBS (including approximately $257.6 million of Agency Interest-Only Strips), approximately $671.0 million of Non-Agency RMBS (including approximately $74.1 million of Non-Agency Interest-Only Strips), approximately $44.2 million Agency CMBS ((including approximately $18.8 million of Agency CMBS Interest-Only Strips), approximately $393.8 million Non-Agency CMBS, approximately $108.9 million of other securities and approximately $7.2 million of residential whole-loans, exclusive of linked transactions. In addition, at December 31, 2014, our linked transactions included approximately $8.2 million of Non-Agency RMBS, approximately $38.6 million of Non-Agency CMBS (including Non U.S. CMBS) and approximately $5.7 million of other securities.

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We use leverage, currently comprised of borrowings under repurchase agreements, as part of our business strategy in order to increase potential returns to stockholders. We accomplish this by borrowing against existing MBS and other securities through repurchase agreements. There are no limits on the maximum amount of leverage that we may use, and we are not required to maintain any particular debt-to-equity leverage ratio under our charter. We may also change our financing strategy and leverage without the consent of stockholders.

As of December 31, 2014, we had entered into master repurchase agreements with 24 counterparties. As of December 31, 2014, we had approximately $3.9 billion of borrowings, including borrowings on linked transactions, outstanding under our repurchase agreements collateralized by approximately $4.4 billion of MBS and other securities. The balance outstanding at December 31, 2014 includes approximately $31.9 million related to linked transactions collateralized by approximately $52.5 million of MBS and other securities and $4.9 million of borrowings related to residential whole-loans owned through trust certificates which are eliminated upon consolidation of approximately $7.2 million. We have entered into swaps to effectively fix the interest rate of our borrowings (for the life of the swap); net of variable-rate payment swaps, of approximately $1.4 billion, under our repurchase agreements, excluding forward starting swaps of $2.2 billion. In addition, as of year-end, we also owned swaptions on approximately an incremental $105.0 million of borrowings. As of December 31, 2014, our aggregate debt-to-equity ratio was approximately 6.3 to 1, including repurchase agreements on linked transactions and 6.2 to 1, excluding repurchase agreements on linked transactions.

Recent Market Conditions and Strategy

Our business is affected by general U.S. residential real estate fundamentals, domestic and foreign commercial real estate fundamentals and the overall U.S. and international economic environment. In particular, our strategy is influenced by the specific characteristics of these markets, including but not limited to prepayment rates and interest rate levels. We expect the results of our operations to be affected by various factors, many of which are beyond our control. Our results of operations will primarily depend on, among other things, the level of our net interest income, the market value of our investment portfolio and the supply of and demand for mortgage-related securities. Our net interest income, which includes the amortization of purchase premiums and accretion of discounts, will vary primarily as a result of changes in interest rates, defaults and severity rates, borrowing costs, and prepayment speeds on our MBS and Target Asset investments. Similarly, the overall value of our investment portfolio will be impacted by these factors as well as changes in the value of residential and commercial real estate and continuing regulatory changes. Over the course of 2014, we have shifted our portfolio to more credit sensitive securities from Agency securities, which we believe given the current economic and interest rate environment will provide a better risk adjusted return.

The current economic and market outlook are shaped in a significant manner by the unprecedented level of fiscal and monetary stimulus that the U.S. Government and U.S. Federal Reserve Board provided in the aftermath of the 2007-2010 financial crisis. The current rate environment is characterized by a flattening yield curve. The U.S. Federal Reserve Board has maintained a near-zero target for the federal funds rate, and has reiterated its commitment to fulfilling its mandate to promote higher growth and lower unemployment and to maintain price stability in the U.S. economy. On January 28, 2015, the U.S. Federal Reserve Board reaffirmed its view that, at the present time, a highly accommodative stance of monetary policy remains appropriate.

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Notwithstanding economic data which suggests continuing improvement in the overall U.S. economy and labor market and the completion by the Federal Reserve of its open market security purchases in October 2014, it is our Manager's view that the significant mortgage debt burden, run-off of fiscal stimulus and budget discipline at both the U.S. federal and state level, the strengthening of the U.S. dollar and general economic weakness in Europe will serve as an impediment to real GDP growth throughout 2015. Real gross domestic product ("GDP") was down sharply in the first quarter of 2014, rebounded substantially in the second and third quarters of 2014, but fell-off in the fourth quarter of 2014. Accordingly, we believe core interest rates will be range bound with slow inflation. For these reasons, and considering its dual mandate to manage both inflation and unemployment, we believe that the U.S. Federal Reserve Board will continue its accommodative monetary policy now in effect. In the press release issued at the conclusion of the Federal Open Market Committee meeting on January 28, 2015, the Federal Reserve stated that in order to support progress toward maximum employment and price stability, the current 0% to 0.25% target range for the federal funds rate remains appropriate. The Federal Reserve went on to say that based on its current assessment of economic conditions, it could be patient in beginning to normalize the stance of monetary policy and even after employment and inflation are near mandate consistent levels, economic conditions may warrant keeping the target federal funds rate below levels considered normal in the longer run. Nevertheless, to the extent the economy improves more quickly, the Federal Reserve would increase the target range for the federal funds rate more quickly and if economic progress is slower than expected, then increases in the target range for the federal funds rate will likely occur later.

As the capital markets have recovered, commercial banks have re-entered the secured lending market, which has quickened the pace of asset recovery, and the return to more normalized credit spreads. Given the current regulatory environment, we continue to see significant non-bank entities filling the void for residential and commercial real estate credit lending. Due to this shift, liquidity in all risk assets has increased. Financing of Agency and Non-Agency RMBS, Agency and Non-Agency CMBS as well as ABS is currently widely available through, among other vehicles, repurchase agreements. Haircuts, or the discount attributed to the value of securities sold under repurchase agreements, range from a low of 3.0% to a high of 5.0% for Agency RMBS, depending on the specific security used as collateral for such repurchase agreements, while haircuts for Agency IOs and IIOs can range from a low of 20% to a high of 25% and haircuts for Non-Agency RMBS and Agency and Non-Agency CMBS range from a low of 13.0% to a high of 60.0% and haircuts for other securities range from a low of 20.0% to a high of 55.0%. Notwithstanding the foregoing, such financing may not be as readily available and at attractive pricing in the future as a result of the increased regulatory capital requirements under the Dodd-Frank Act and Basel III.

In response to the financial crisis, the U.S. government, through the FHA, the Federal Deposit Insurance Corporation, or FDIC, and the U.S. Treasury, has commenced or proposed implementation of programs designed to provide homeowners with assistance in avoiding residential mortgage loan foreclosures. These loan modification and refinance programs, future U.S. federal, state and/or local legislative or regulatory actions that result in the modification of outstanding mortgage loans, as well as changes in the requirements necessary to qualify for refinancing mortgage loans with FNMA, FHLMC or GNMA, may adversely affect the value of, and the returns on, residential mortgage loans, RMBS, real estate-related securities and various other asset classes in which we may invest. In addition to the foregoing, the U.S. Congress and/or various states and local legislators may enact additional legislation or regulatory action, such as the recently enacted qualifying mortgage requirements under the Dodd-Frank Act, to address the current economic crisis or for other purposes that could have a material adverse effect on lending in general and our ability to execute our business strategies. In particular, we believe that while the recently enacted qualifying mortgage requirements under the Dodd-Frank Act may present an opportunity to acquire and securitize certain "non-qualifying" or Non-QM mortgages, it is likely to reduce the overall production of new mortgages, thereby negatively impacting the general supply of RMBS.

On January 4, 2012, the U.S. Federal Reserve Board released a report titled *"The U.S. Housing Market: Current Conditions and Policy Considerations"* to Congress providing a framework for thinking about certain issues and tradeoffs that policy makers might consider. In March 2014, Senate Banking Committee Chairman Tim Johnson and Ranking Member Mike Crapo announced an agreement on their own version of GSE reform which would eventually replace FNMA and FHLMC with a new system. It is unclear how future legislation may impact the housing finance market and the investing environment for agency securities as the method of reform is undecided and has not yet been defined by the regulators.

Critical Accounting Policies

The consolidated financial statements include our accounts, those of our consolidated subsidiary, our wholly owned taxable REIT subsidiary or "TRS" and a variable interest entity ("VIE") related to the acquisition of residential whole-loans in which we are the primary beneficiary. All intercompany amounts have been eliminated in consolidation. In accordance with GAAP, our consolidated financial statements require the use of estimates and assumptions that involve the exercise of judgment and use of assumptions as to future uncertainties. In accordance with SEC guidance, the following discussion addresses the accounting policies that we currently apply. Our most critical accounting policies will involve decisions and assessments that could affect our reported assets and liabilities, as well as our reported revenues and expenses. We believe that all of the decisions and assessments upon which our consolidated financial statements have been based were reasonable at the time made and based upon information available to us at that time. We have identified what we believe will be our most critical accounting policies to be the following:

Investments

We elected the fair value option for all of our MBS, other securities and whole-loans at the date of purchase, which permits us to measure these securities at fair value with the change in fair value included as a component of earnings. Although we have elected the fair value option for our MBS, other securities and whole-loans, we separately compute interest income on our MBS, other securities and whole-loans under the prescribed method based on the nature of the investment. As such, premiums and discounts are amortized or accreted into interest income and are included in Interest income in the Consolidated Statements of Operations.

Valuation of financial instruments

We disclose the fair value of our financial instruments according to a fair value hierarchy (Levels I, II, and III, as defined below). In accordance with GAAP, we are required to provide enhanced disclosures regarding instruments in the Level III category (which require significant management judgment), including a separate reconciliation of the beginning and ending balances for each major category of assets and liabilities. GAAP establishes a framework for measuring fair value in accordance with GAAP and expands financial statement disclosure requirements for fair value measurements. GAAP further specifies a hierarchy of valuation techniques, which is based on whether the inputs into the valuation technique are observable or unobservable. The hierarchy is as follows:

Level I Quoted prices in active markets for identical assets or liabilities.

Level II Quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level III Prices are determined using significant unobservable inputs. In situations where quoted prices or observable inputs are unavailable (for example, when there is little or no market activity for an investment at the end of the period), unobservable inputs may be used.

The level in the fair value hierarchy within which a fair measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

When available, we use quoted market prices to determine the fair value of an asset or liability. If quoted market prices are not available, we consult with independent pricing services or obtain third party broker quotes. If independent pricing service, or third party broker quotes are not available, we determine the fair value of the securities using valuation techniques that use, when possible, current market-based or independently-sourced market parameters, such as interest rates.

While linked transactions are treated as derivatives for GAAP, the securities underlying the Company's linked transactions are valued using similar techniques to those used for our securities portfolio. The value of the underlying security is then netted against the carrying amount (which approximates fair value) of the repurchase agreement at the valuation date. Additionally, TBA instruments are similar in substance to our Agency RMBS portfolio, and the Company therefore estimates fair value based on similar methods.

We determine the fair value of derivative financial instruments by obtaining quotes from a third party pricing service, whose pricing is subject to review by our Manager's pricing committee. In valuing our interest rate derivatives, such as swaps and swaptions, we consider the creditworthiness of our counterparties, along with collateral provisions contained in each derivative agreement, from the perspective of both us and our counterparties. All of our interest rate swaps are either cleared through a central clearing house and subject to the clearing house margin requirements or subject to bilateral collateral arrangements with the vast majority of interest rate swaps entered into beginning in September 2013 being cleared through a central clearing house. We also have netting arrangements in place with all derivative counterparties pursuant to standard documentation developed by the International Swap and Derivatives Association. Consequently, no credit valuation adjustment was made in determining the fair value of interest rate derivatives.

Valuation techniques for MBS, whole-loans and other structured securities may be based upon models that consider the estimated cash flows of the security. Depending on the security and the underlying collateral, the primary inputs to the model include yields for to-be-announced (also known as TBAs) Agency RMBS, the U.S. Treasury market and floating rate indices such as LIBOR, the Constant Maturity Treasury rate and the prime rate as a benchmark yield. In addition, the model may incorporate the current weighted average maturity and additional pool level information such as prepayment speeds, default frequencies and default severities, if applicable. To the extent, the inputs are observable and timely, the securities are categorized in Level II of the fair value hierarchy; otherwise, unless alternative pricing information as described is available, they are categorized as Level III.

Fair value under GAAP represents an exit price in the normal course of business, not a forced liquidation price. If we are forced to sell assets in a short period to meet liquidity needs, the prices we receive could be substantially less than the recorded fair values of our assets. Furthermore, the analysis of whether it is more likely than not that we will be required to sell securities in an unrealized loss position prior to an expected recovery in value (if any), the amount of such expected required sales, and the projected identification of which securities will be sold is also subject to significant judgment, particularly in times of market illiquidity.

We will review any changes to the valuation methodology to ensure the changes are appropriate. The methods used may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while we anticipate that our valuation methods will be appropriate and consistent with other market participants, the use of different methodologies, or assumptions, to determine the fair value of certain financial instruments can result in a different estimate of fair value at the reporting date. We use inputs that are current as of the measurement date, which may include periods of market dislocation, during which price transparency may be reduced.

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All valuations received from independent pricing services are non-binding. We primarily utilize an independent third party pricing service as the primary source for valuing the Company's assets.

We generally receive one independent pricing service price for each investment in our portfolio. Our Manager has established a process to review and validate the pricing received from the independent pricing service and has a process for challenging prices received from the independent pricing service when necessary. The Company utilizes our Manager's policies in this regard. Our and our Manager's review of the independent third party pricing data may consist of a review of the daily change in the prices provided by the independent pricing vendor which exceed established tolerances or comparisons to executed transaction prices. Our Manager's pricing group, which functions independently from its portfolio management personnel, corroborates the price differences or changes in price by comparing the vendor price to alternate sources including other independent pricing services or broker quotations. If the price change or difference cannot be corroborated, the Manager's pricing group consults with the portfolio management team for market color in reviewing such pricing data as warranted. To the extent that our Manager has information, typically in the form of broker quotations that would indicate that a price received from the independent pricing service is outside of a tolerance range, our Manager generally challenges the independent pricing service price.

To ensure proper fair value hierarchy, we and our Manager review the methodology used by the third party pricing service to understand whether observable market data is being utilized in the vendor's pricing methodology. Generally, this review is conducted annually, however ad-hoc reviews of the pricing methodology and the data do occur. The review of the assumptive data received from the vendor includes comparing key inputs. In addition, as part of our regular review of pricing, our Manager's pricing group may have informal discussions with the independent pricing vendor regarding their evaluation methodology or the market data utilized in their determination as well as performing back testing with regard to the sale of certain securities. The conclusion that a price should be overridden in accordance with our Manager's pricing methodology may impact the fair value hierarchy of the security for which such price has been adjusted.

Linked transactions

In instances where we finance the acquisition of securities through repurchase agreements with the same counterparty from which the securities were purchased, we evaluate such transactions in accordance with GAAP. This guidance requires the initial transfer of a financial asset and repurchase financing that are entered into contemporaneously with, or in contemplation of, one another to be considered linked unless all of the criteria found in the guidance are met at the inception of the transaction. If the transaction meets all of the conditions, the initial transfer shall be accounted for separately from the repurchase financing, and we will record the securities and the related financing on a gross basis on our Consolidated Balance Sheets with the corresponding interest income and interest expense in our Consolidated Statements of Operations. If the transaction is determined to be linked, we will record the initial transfer and repurchase financing on a net basis and record a forward commitment to purchase securities as a derivative instrument with changes in market value being recorded on our Consolidated Statements of Operations. Such forward commitments are recorded at fair value with subsequent changes in fair value recognized in Gain (loss) on linked transactions, net on our Consolidated Statements of Operations. We refer to these transactions as Linked Transactions. When or if a transaction is no longer considered to be linked, the security and related repurchase financing will be reported on a gross basis. The unlinking of a transaction causes a realized event in which the fair value of the security as of the date of unlinking will become the cost basis of the security. The difference between the fair value on the unlinking date and the existing cost basis of the security will be the realized gain or loss. Recognition of effective yield for such security will be calculated prospectively using the new cost basis. For linked transactions, we reflect purchases and sales of securities within the investing section of our Consolidated Statements of Cash Flows. Proceeds from repurchase agreements borrowings and repayments of repurchase agreement borrowings are reflected in the financing section of our Consolidated Statements of Cash Flows.

The securities underlying our linked transactions are valued using similar techniques to those used for our securities portfolio.

Starting in 2015, GAAP will no longer require us to segregate and treat linked transactions as derivatives. Accordingly, we will report such securities and the corresponding repurchase agreement on a gross basis on our Consolidated Balance Sheets and with the corresponding interest income and interest expense reported in our Consolidated Statements of Operations. See "Recent accounting pronouncements" for details.

Interest income recognition and Impairment

Agency MBS and Non-Agency MBS, excluding Interest-Only Strips, and other securities rated AA and higher at the time of purchase

Interest income on mortgage-backed securities and other securities is accrued based on the respective outstanding principal balances and their corresponding contractual terms. Premiums and discounts associated with Agency MBS and Non-Agency MBS, excluding Interest-Only Strips, and other securities rated AA and higher at the time of purchase are amortized into interest income over the estimated life of such securities using the effective yield method. Adjustments to premium and discount amortization are made for actual prepayment activity. On at least a quarterly basis, we estimate prepayments for our securities and, as a result, if prepayments increase (or are expected to increase), we will accelerate the rate of amortization (accretion) on premiums or discounts and make a retrospective adjustment to historical amortization (accretion). Alternatively, if prepayments decrease (or are expected to decrease) we will reduce the rate of amortization (accretion) on the premiums or discounts and make a retrospective adjustment to historical amortization.

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Our conversion to a new accounting system in the calculation methodology used to determine the amortization of bond premium on our Agency MBS portfolio as of April 1, 2014, resulted in a change in estimate of approximately $1.2 million. The impact of this change of estimate was limited to an increase of $0.03 per share in core earnings (a non-GAAP measure). For financial reporting purposes, the impact of the change in estimate had no impact on Net income and was limited to an increase of approximately $1.2 million to Interest Income and an equal offsetting reduction to Unrealized gain (loss) on Mortgage-backed securities, other securities and whole-loans, net on the Consolidated Statements of Operations. We do not believe the aforementioned change in estimate will have a material impact to subsequent periods.

A decline in the fair market value of our assets may require us to recognize an "other-than-temporary" impairment against such assets under GAAP unless we were to determine that, with respect to any assets in unrealized loss positions, we do not have the intent to sell these investments, it is more likely than not that we will not be required to sell the investment before recovery of a security's amortized cost basis and we will not be required to sell the security for regulatory or other reasons. In addition, an other-than-temporary impairment is deemed to have occurred when there is an adverse change in the expected cash flows (principal or interest) to be received and the fair value of the security is less than its carrying amount. In determining whether an adverse change in cash flows occurred, the present value of the remaining cash flows, as estimated at the initial transaction date (or the last date previously revised), is compared to the present value of the expected cash flows at the current reporting date. The estimated cash flows reflect those a "market participant" would use and are discounted at a rate equal to the current yield used to accrete interest income. If such a determination is made, we would recognize unrealized losses through earnings and write down the amortized cost of such assets to a new cost basis, based on the fair value of such assets on the date they are considered to be other-than-temporarily impaired. Other than for "plain-vanilla" variable rate Non-Agency MBS, we do not bifurcate the loss between credit loss and loss attributed to change in interest rates, therefore, the entire loss is recorded as other-than-temporary. Such impairment charges reflect non-cash losses at the time of recognition; subsequent disposition or sale of such assets can further affect our future losses or gains, as they are based on the difference between the sales price received and adjusted amortized cost of such assets at the time of sale.

The determination of whether an other-than-temporary impairment exists is subject to management's estimates based on consideration of both factual information available at the time of assessment as well as our estimates of the future performance and projected amount and timing of cash flows expected to be collected on the security. As a result, the timing and amount of an other-than-temporary impairment constitutes an accounting estimate that may change materially over time.

Non-Agency MBS and other securities that are rated below AA at the time of purchase and Interest-Only Strips that are not classified as derivatives

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Interest income on Non-Agency MBS and other securities that are rated below AA at the time of purchase and Interest-Only Strips that are not classified as derivatives, are recognized based on the effective yield method. The effective yield on these securities is based on the projected cash flows from each security, which is estimated based on our observation of the then current market information and events and will include assumptions related to interest rates, prepayment rates and the timing and amount of credit losses. On at least a quarterly basis, we review and, if appropriate, make adjustments to our cash flow projections based on input and analysis received from external sources, internal models, and our judgment about interest rates, prepayment rates, the timing and amount of credit losses (if applicable), and other factors. Where appropriate, we may include in our cash flow projections the U.S Department of Justice's settlements with the major residential mortgage originators, regarding certain lending practices. Changes in cash flows from those originally projected, or from those estimated at the last evaluation, may result in a prospective change in the yield/interest income recognized on such securities. Actual maturities of the securities are affected by the contractual lives of the associated mortgage collateral, or mortgages, periodic payments of scheduled principal, and prepayments of principal. Therefore, actual maturities of the securities will generally be shorter than stated contractual maturities.

Based on the projected cash flows from any Non-Agency MBS and other structured security, which we may purchase at a discount to par value, a portion of the purchase discount may be designated as credit protection against future credit losses and, therefore, not accreted into interest income. The amount designated as credit discount may be adjusted over time, based on the actual performance of the security, its underlying collateral, actual and projected cash flow from such collateral, economic conditions and other factors. If the performance of a security with a credit discount is more favorable than forecasted, a portion of the amount designated as credit discount may be accreted into interest income prospectively.

In addition, an other-than-temporary impairment is deemed to have occurred when there is an adverse change in the expected cash flows (principal or interest) to be received and the fair value of the beneficial interest is less than its carrying amount. In determining whether an adverse change in cash flows occurred, the present value of the remaining cash flows, as estimated at the initial transaction date (or the last date previously revised), is compared to the present value of the expected cash flows at the current reporting date. The estimated cash flows reflect those a "market participant" would use and are discounted at a rate equal to the current yield used to accrete interest income. The Company does not bifurcate the loss between credit loss and loss attributed to change in interest rates, therefore, the entire loss is recorded as other-than-temporary. These adjustments are reflected in our Consolidated Statements of Operations as Other loss on Mortgage-backed securities and other securities.

Securities denominated in a foreign currency contain additional risk in that the amortized cost basis for those securities may not be recovered due to declines in currency exchange rates. We consider the length of time that the security's fair value has declined due to the decline in foreign exchange rates, when assessing other-than temporary impairment. We entered into foreign currency swaps and forwards in order to hedge our exposure to changes in foreign currency exchange rates.

Following the recognition of an other-than-temporary impairment, a new amortized cost basis is established for the security. However, to the extent that there are subsequent increases in cash flows expected to be collected, the other-than-temporary impairment previously recorded may be accreted back through interest income via increased yield.

The determination of whether an other-than-temporary impairment exists is subject to management's estimates based on consideration of both factual information available at the time of assessment as well as our estimates of the future performance and projected amount and timing of cash flows expected to be collected on the security. As a result, the timing and amount of an other-than-temporary impairment constitutes an accounting estimate that may change materially over time.

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Residential whole-loans

We record our purchases of residential whole-loans as the amount paid to the seller plus any fees paid or less any fees received. All other costs incurred in connection with acquiring purchased residential whole-loans or committing to purchased residential whole-loans are charged to expense as incurred. We amortize or accrete any premium or discount over the life of the related loan utilizing the effective interest method, using the contractual payments terms of the loans. On at least a quarterly basis, we evaluate the collectability of both interest and principal of each loan, if circumstances warrant, to determine whether they are impaired. A loan is impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the existing contractual terms. When a loan is impaired, we do not record a loss accrual as we have elected the fair value option. However, income recognition is suspended for loans at the earlier of the date at which payments become 90-days past due or when, in the opinion of management, a full recovery of income and principal becomes doubtful. When the ultimate collectability of the principal of an impaired loan is in doubt, all payments are applied to principal under the cost recovery method. When the ultimate collectability of the principal of an impaired loan is not in doubt, contractual interest is recorded as interest income when received, under the cash basis method until an accrual is resumed when the loan becomes contractually current and performance is demonstrated to be resumed. A loan is written off when it is no longer realizable and/or legally discharged.

Foreign currency transactions

We have and expect to continue to enter into transactions denominated in foreign currency from time to time. At the date the transaction is recognized, the asset and/or liability will be measured and recorded using the exchange rate in effect at the date of the transaction. At each balance sheet date, such foreign currency assets and liabilities are re-measured using the exchange rate in effect at the date of the balance sheet, resulting in unrealized foreign currency gains or losses. Unrealized foreign currency gains or losses on MBS and other securities are recorded in Unrealized gain (loss) on Mortgage-backed securities, other securities and whole-loans, net on the Consolidated Statements of Operations. In addition, we evaluate whether an other-than-temporary impairment is deemed to have occurred on MBS and other securities denominated in a foreign currency. Cash flows from MBS and other securities denominated in foreign currencies are received in a foreign currency, and as a result, we may incur a loss due to changes in foreign exchange rates even when all contractual cash flows are received. These adjustments are reflected in our Consolidated Statements of Operations as Other loss on Mortgage-backed securities and other securities. Unrealized and realized foreign currency gains or losses on borrowings under repurchase agreements are recorded in Interest income on cash balances and other income (loss), net on the Consolidated Statements of Operations. Interest income from investments denominated in a foreign currency and interest expense on borrowings denominated in a foreign currency are recorded at the average rate of exchange during the period.

Variable Interest Entities ("VIEs")

VIEs are defined as entities in which equity investors either do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support, are unable to direct the entity's activities or are not exposed to the entity's losses or entitled to its residual returns. VIEs are required to be consolidated by their primary beneficiary. The primary beneficiary of a VIE is determined to be the party that has both the power to direct the activities of a VIE that most significantly impact the VIE's economic performance and the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. This determination of the requirement to consolidate a VIE and the requirement to disclose information about our involvement in a VIE can sometimes involve complex and subjective analyses. Ongoing assessments of whether an enterprise is the primary beneficiary of a VIE is required.

Due from counterparties/Due to counterparties

Due from counterparties represents cash posted by us with our counterparties as collateral for our interest rate and/or currency derivative financial instruments, repurchase agreements, and TBAs. Due to counterparties represents cash posted with us by our counterparties as collateral under our interest rate and/or currency derivative financial instruments, repurchase agreements, and TBAs. In addition, as provided below, Due to counterparties may include non-cash collateral in which we have the obligation to return the collateral upon us either selling or pledging the non-cash collateral. To the extent we receive collateral other than cash from our counterparties such assets are not included in our Consolidated Balance Sheets. Notwithstanding the foregoing, if we either rehypothecate such assets or pledge the assets as collateral pursuant to a repurchase agreement, the cash received and the corresponding liability is reflected on our Consolidated Balance Sheets.

Derivatives and hedging activities

Subject to maintaining our qualification as a REIT for U.S. federal income tax purposes, we utilize derivative financial instruments to hedge the interest rate risk associated with our borrowings and the currency risk associated with our non U.S. dollar denominated investments. Derivatives, subject to the REIT requirements, are used for hedging purposes including overall market risk. We determine their fair value and obtain quotations from a third party to facilitate the process of determining such fair values. If our hedging activities do not achieve the desired results, reported earnings may be adversely affected.

GAAP requires an entity to recognize all derivatives as either assets or liabilities on the Consolidated Balance Sheets and to measure those instruments at fair value. If the reporting entity does not elect hedge accounting for a derivative instrument, fair value adjustments are recorded in earnings immediately.

We elected not to apply hedge accounting for our derivative instruments and, accordingly record the change in fair value and net interest rate swap payments (including accrued amounts) related to interest rate swaps in Gain (loss) on derivative instruments, net in our Consolidated Statements of Operations. Similarly, the change in fair value and net currency payment (including accrued amounts) related to our currency hedges will also be included in Gain (loss) on derivative instruments net in our Consolidated Statements of Operations. In our Consolidated Statements of Cash Flows, premiums received and paid on termination of our interest rate swaps, excluding interest rate swaps containing an other-than-insignificant financing element and the unamortized premium of market agreed coupon ("MAC") interest rate swaps, are included in cash flows from operating activities. On the other hand, proceeds and payments on settlement of swaptions, mortgage put options, futures contracts and TBAs are included in cash flows from investing activities. Proceeds and payments on settlement of forward contracts are reflected in cash flows from financing activities in our Consolidated Statement of Cash Flows. While payments made at the time of entering MAC interest rate swaps are included in cash flows from investing activities, payments received by us upon entering MAC interest rate swaps are included in either cash flows from investing activities or cash flows financing activities, depending on whether or not the derivative instrument includes an other-than-insignificant financing element. For MAC interest rate swaps containing an other-than-insignificant financing element, all cash flows over the life of the derivative are treated as cash flows from financing activities. Return and recovery of basis activity for MAC interest rate swaps is included in cash flows from investing activities for swaps not containing an other-than-insignificant financing element in our Consolidated Statement of Cash Flows. For Agency and Non-Agency Interest-Only Strips accounted for as derivatives, the purchase, sale and recovery of basis activity is included with MBS and other securities under cash flows from investing activities in our Consolidated Statement of Cash Flows.

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We also invest in Agency and Non-Agency Interest-Only Strips, swaptions, mortgage put options, futures contracts and TBAs. We evaluate the terms and conditions of our holdings of Agency and Non-Agency Interest-Only Strips, swaptions mortgage put options, futures contracts and TBAs to determine if these instruments have the characteristics of an investment or should be considered a derivative under GAAP. In determining the classification of our holdings of Interest-Only Strips, we evaluate the securities to determine if the nature of the cash flows has been altered from that of the underlying mortgage collateral. Generally, a security which represents a strip off of a mortgage pass through security will be considered a hybrid instrument classified as a MBS investment on our Consolidated Balance Sheets utilizing the fair value option. Alternatively, Interest-Only Strips, for which the underlying mortgage collateral has been included into a structured security that alters the cash flows from the underlying mortgage collateral, are accounted for as derivatives at fair value. Accordingly, Agency and Non-Agency Interest-Only Strips, swaptions, mortgage put options, futures contracts and TBAs having the characteristics of derivatives are accounted for at fair value with such changes recognized in Gain (loss) on derivative instruments, net in our Consolidated Statements of Operations, along with any interest earned (including accrued amounts). The carrying value of the Agency and Non-Agency Interest-Only Strips, accounted for as derivatives, is included in Mortgage-backed securities on the Consolidated Balance Sheets. The carrying value of interest rate swaptions, mortgage put options, currency forwards, futures contracts and TBAs is included in Derivative assets or Derivative liabilities on the Consolidated Balance Sheets.

We evaluate all of our financial instruments to determine if such instruments are derivatives or contain features that qualify as embedded derivatives. An embedded derivative is separated from the host contact and accounted for separately when all of the guidance criteria are met. Hybrid instruments that are remeasured at fair value through earnings, including the fair value option, are not bifurcated. Our derivative instruments also include linked transactions, which reflect a forward commitment to purchase assets. Derivative instruments are recorded at fair value and are re-valued at each reporting date, with changes in the fair value together with interest earned (including accrued amounts) reported in Gain (loss) on derivative instruments, net in our Consolidated Statements of Operations. While accounted for as derivative instruments, linked transactions, including changes in fair value and interest earned (including accrued amounts) are reported separately in our Consolidated Balance Sheets, Consolidated Statements of Operations and Consolidated Statements of Cash Flows.

Repurchase agreements

Mortgage-backed securities and other securities sold under repurchase agreements are treated as collateralized financing transactions, unless they meet sales treatment. Securities financed through a repurchase agreement remain on our Balance Sheet as an asset and the amount of cash received from the lender is recorded in our Consolidated Balance Sheets as a liability. Interest payable in accordance with repurchase agreements is recorded as accrued interest payable on the Consolidated Balance Sheets. Interest paid in accordance with repurchase agreements is recorded as interest expense.

In instances where we pledge securities through repurchase agreements with the same counterparty from which the securities are purchased, we will account for the purchase commitment and repurchase agreement on a net basis and record a forward commitment to purchase securities as a derivative instrument if the transaction does not comply with the criteria for gross presentation. Such forward commitments will be recorded at fair value with subsequent changes in fair value recognized in income. If the transaction complies with the criteria for gross presentation, we will record the assets and the related financing on a gross basis in our Consolidated Balance Sheets and the corresponding interest income and interest expense in our Consolidated Statements of Operations. Starting in 2015, we will no longer be required to treat such assets as linked transactions and will report the security and corresponding repurchase financing on a gross basis, see "Recent accounting pronouncements" for details.

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Share-based compensation

We account for share-based compensation to our independent directors, to our officers and employees, to our Manager and to employees of our Manager and its affiliates using the fair value based methodology prescribed by GAAP. Compensation cost related to restricted common stock issued to our independent directors and employees is measured at its fair value at the grant date, and amortized into expense over the service period on a straight-line basis. Compensation cost related to restricted common stock issued to our Manager and to employees of our Manager and its affiliates is initially measured at fair value at the grant date, and re-measured at fair value on subsequent dates to the extent the awards are unvested and the change in fair value is reported in the Consolidated Statements of Operations as non-cash stock based compensation.

Warrants

We account for the warrants comprising a part of the units issued in the private placement to certain institutional accredited investors concurrent with our IPO in accordance with Accounting Standards Codification 815, Accounting for Derivative Instruments and Hedging Activities, which provides guidance on the specific accounting treatment of a multitude of derivative instruments. We have evaluated the warrants issued by us and have recorded the warrants at their relative fair value as a component of equity, using a variation of the adjusted Black-Scholes option valuation model at their time of issuance.

Income taxes

We operate and have elected to be taxed as a REIT commencing with our taxable year ended December 31, 2012. Accordingly, we will generally not be subject to corporate U.S. federal or state income tax to the extent that we make qualifying distributions to our stockholders, and provided that we satisfy on a continuing basis, through actual investment and operating results, the REIT requirements including certain asset, income, distribution and stock ownership tests. If we fail to qualify as a REIT, and do not qualify for certain statutory relief provisions, we will be subject to U.S. federal, state and local income taxes and may be precluded from qualifying as a REIT for the subsequent four taxable years following the year in which we lost our REIT qualification. Accordingly, our failure to qualify as a REIT could have a material adverse impact on our results of operations and amounts available for distribution to our stockholders.

Our dividends paid deduction for qualifying dividends paid to our stockholders is computed using our taxable income calculated in accordance with the REIT requirements as opposed to net income reported on the consolidated financial statements. Taxable income, generally, will differ from net income reported on the consolidated financial statements because the determination of taxable income is based on tax provisions and not financial accounting principles.

We may elect to treat certain of our subsidiaries as TRSs. In general, a TRS of ours may hold assets and engage in activities that we cannot hold or engage in directly and generally may engage in any real estate or non-real estate-related business. A TRS is subject to U.S. federal, state and local corporate income taxes. While a TRS will generate net income, a TRS can declare dividends to us, which will be included in our taxable income and necessitate a distribution to our stockholders. The portion of our dividends, if any, pertaining to distributions from a TRS may be treated as qualified dividend dividends. Conversely, if we retain earnings at the TRS level, no distribution is required and we can increase book equity of the consolidated entity. As of December 31, 2014, we have a single wholly owned subsidiary which we have elected to treat as a TRS. We had a cumulative taxable loss in our TRS for the year ended December 31, 2014. As there can be no certainty that the TRS will have taxable income in the future, no tax benefit was included in our consolidated financial statements as of such date.

We evaluate uncertain tax positions, if any, and classify interest and penalties, if any, related to unrecognized tax benefits as a component of the provision for income taxes.

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Accounting standards applicable to emerging growth companies

The JOBS Act contains provisions that relax certain requirements for "emerging growth companies" for which we qualify. For as long as we are an emerging growth company, which may be up to five full fiscal years, unlike other public companies, we will not be required to: (i) comply with any new or revised financial accounting standards applicable to public companies until such standards are also applicable to private companies under Section 102(b)(1) of the JOBS Act; (ii) provide an auditor's attestation report on management's assessment of the effectiveness of our system of internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act; (iii) comply with any new requirements adopted by the PCAOB requiring mandatory audit firm rotation or a supplement to the auditor's report in which the auditor would be required to provide additional information about the audit and the financial statements of the issuer; or (iv) comply with any new audit rules adopted by the PCAOB after April 5, 2012 unless the SEC determines otherwise. We currently take advantage of some of such exemptions. Our qualification for remaining an emerging growth company under the five full fiscal years expires on December 31, 2018. However, we may no longer qualify sooner if our gross revenues for any year equal $1.0 billion or more, we issued more than $1.0 billion in non-convertible debt during the three previous years, or on the date in which we are deemed to be a large accelerated filer.

As noted above, under the JOBS Act, emerging growth companies can delay adopting new or revised accounting standards that have different effective dates for public and private companies until such time as those standards apply to private companies. We currently take advantage of such extended transition period. Since we are not required to comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for other public companies, our financial statements may not be comparable to the consolidated financial statements of companies that comply with public company effective dates. If we were to elect to comply with these public company effective dates, such election would be irrevocable pursuant to Section 107 of the JOBS Act.

Recent accounting pronouncements

Accounting Standards to be Adopted in Future Periods

In April 2014, the Financial Accounting Standards Board issued updated guidance that changes the requirements for reporting discontinued operations. Under the new guidance, a discontinued operation is defined as a disposal of a component of an entity or group of components of an entity that is disposed of or is classified as held for sale and represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results. The guidance is effective prospectively as of the first quarter of 2015, with early adoption permitted for new disposals or new classifications as held-for-sale. The guidance is effective for annual periods beginning on or after December 15, 2014 and interim periods within annual periods beginning on or after December 15, 2015. Early adoption is permitted but only for disposals (or classifications as held for sale) that have not been reported in financial statements previously issued or available for issue. The new guidance is not expected to have a material impact on our consolidated financial statements.

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In June 2014, the Financial Accounting Standards Board issued guidance that changes the accounting for repurchase-to-maturity transactions and repurchase financing arrangements. The new guidance aligns the accounting for repurchase-to-maturity transactions and repurchase agreements executed as a repurchase financing with the accounting for other typical repurchase agreements. These transactions would all be accounted for as secured borrowings. The guidance eliminates sale accounting for repurchase-to-maturity transactions and supersedes the guidance under which a transfer of a financial asset and a contemporaneous repurchase financing could be accounted for on a combined basis as a forward agreement, which has resulted in outcomes referred to as off-balance-sheet accounting. In addition, the guidance requires additional disclosures. The guidance is effective for the first interim or annual period beginning after December 15, 2014. Earlier application for a public company is prohibited. Certain disclosures under this guidance do not take effect until the first period beginning after March 15, 2015.We currently account for certain transfers as forward agreements under the existing guidance, which are currently classified as linked transactions. The new guidance will require us to record these transfers as secured borrowings. The implementation of the new guidance will result in a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption. The new guidance is not expected to have a material impact on our consolidated financial statements.

In August 2014, the Financial Accounting Standards Board issued guidance that will require an entity's management to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. According to the new guidance, substantial doubt exists when conditions and events, considered in the aggregate, indicate that it is probable that the entity will be unable to meet its obligations as they become due within one year after the date the financial statements are issued. The term "probable" is used consistently with its current use in U.S. GAAP for loss contingencies. Disclosures will be required if conditions give rise to substantial doubt about the entity's ability to continue as a going concern, including whether management's plans that are intended to mitigate those conditions will alleviate the substantial doubt when implemented. The guidance is effective for annual periods ending after December 15, 2016. Early application is permitted. Our first assessment under the new guidance will be completed for the year ending December 31, 2016.

In January 2015, the FASB issued guidance to simplify income statement presentation by eliminating the concept of extraordinary items. U.S. GAAP currently requires that a company separately classify, disclose and present extraordinary events and transactions. The guidance eliminates the concept of extraordinary items from U.S. GAAP. Under the existing guidance, an entity is required to separately disclose extraordinary items, net of tax, in the income statement after income from continuing operations if an event or transaction is of an unusual nature and occurs infrequently. This separate, net-of-tax presentation (and corresponding earnings per share impact) will no longer be allowed. The existing requirement to separately present items that are of an unusual nature or occur infrequently on a pre-tax basis within income from continuing operations has been retained. The new guidance also requires similar separate presentation of items that are both unusual and infrequent. The standard is effective for periods beginning after December 15, 2015. Early adoption is permitted, but only as of the beginning of the fiscal year of adoption. Upon adoption, a reporting entity may elect prospective or retrospective application. If adopted prospectively, both the nature and amount of any subsequent adjustments to previously reported extraordinary items must be disclosed. The new guidance is not expected to have a material impact on our consolidated financial statements.

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In February 2015, the FASB issued guidance to simplify and reduce the number of consolidation models through the elimination of an indefinite deferral for certain entities and by placing more emphasis on risk of loss when determining a controlling financial interest. The guidance affects reporting entities that are required to evaluate whether they should consolidate certain legal entities. All legal entities are subject to reevaluation under the revised consolidation model. The standard is effective for fiscal years, and for interim periods within fiscal years beginning after December 15, 2015. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. We are currently assessing the impact that this guidance will have on our consolidated financial statements when adopted.

Results of Operations

The following discussion of our results of operations highlights our performance for the years ended December 31, 2014 and December 31, 2013 and for the period from May 15, 2012 (commencement of operations) through December 31, 2012. For the year ended December 31, 2014, we had net income of $100.7 million or $2.67 per basic and diluted weighted average common share. For the year ended December 31, 2013, we had a net loss of $27.9 million or $1.19 per basic and diluted weighted average common share. From May 15, 2012 (commencement of operations) through December 31, 2012, we had net income of $57.3 million or $3.64 per basic and $3.63 diluted weighted average common share. During the later portion of 2013, and continuing through 2014 we expanded our investment in Non-Agency MBS and commenced investing in CMBS and other credit oriented structured securities and adjusted our overall leverage and hedging strategy pursuant to our current business plan. Accordingly, operating results for the partial period from May 15, 2012 through December 31, 2012 may not to be fully comparable with the results of our operations for the full years ended December 31, 2014 and December 31, 2013.

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Investments

The following table presents certain information about our investment portfolio at December 31, 2014 which is a Non-GAAP measure due to the inclusion of our Linked Transactions, in order to present a complete economic presentation of our portfolio, which is reconciled to GAAP below, as follows (dollars in thousands):

	Principal Balance	Unamortized Premium (Discount)	Discount Designated as Credit Reserve and OTTI	Amortized Cost	Unrealized Gain (Loss)	Fair Value	Net Weighted Average Coupon(1)
Agency RMBS 20-Year Mortgage							
Coupon Rate:							
3.00%	$ 319,017	$ 14,769	$	$ 333,786	$ (4,038)	$ 329,748	3.0%
3.50%	130,766	7,233		137,999	(93)	137,906	3.5%
4.00%	605,081	34,614		639,695	12,682	652,377	4.0%
	1,054,864	56,616		1,111,480	8,551	1,120,031	3.6%
30-Year Mortgage							
Coupon Rate:							
3.50%	542,093	37,177		579,270	(12,353)	566,917	3.5%
4.00%	468,487	38,609		507,096	(1,915)	505,181	4.0%
4.50%	571,270	42,450		613,720	17,994	631,714	4.5%
5.50%	68,043	8,712		76,755	792	77,547	5.5%
6.00%	7,747	928		8,675	185	8,860	6.0%
	1,657,640	127,876		1,785,516	4,703	1,790,219	4.1.%
Agency RMBS IOs and IIOs(2)	N/A	N/A		178,162	10,344	188,506	4.0%
Agency and Non-Agency IOs and IIOs accounted for as derivatives(2)(3)	N/A	N/A	N/A	N/A	N/A	88,229	2.9%
	N/A	N/A		178,162	10,344	276,735	3.5%
Non-Agency RMBS	764,431	11,525	(181,203)	594,753	10,319	605,072	3.8%
Non-Agency RMBS IOs and IIOs	N/A	N/A	N/A	61,144	8,511	69,655	6.1%
	764,431	11,525	(181,203)	655,897	18,830	674,727	4.5%
Agency and Non-Agency CMBS, including Non U.S.	491,271	(31,216)	(3,124)	456,931	804	457,735	5.4%
CMBS Interest-Only Strips	N/A	N/A	N/A	4,017	98	4,115	4.8%
	491,271	(31,216)	(3,124)	460,948	902	461,850	5.4%
Other securities(4)	109,423	(691)		116,135	(1,490)	114,645	4.6%
Residential whole-loans	7,034	93		7,127	93	7,220	5.7%
Total: Non GAAP Basis-Including Linked Transaction	4,084,663	164,203	(184,327)	4,315,265	41,933	4,445,427	4.0%
Linked Transactions, including Non U.S.	54,117	3,194	(2,320)	54,991	(2,507)	52,484	8.6%
Total: GAAP Basis	$ 4,030,546	$ 161,009	$ (182,007)	$ 4,260,274	$ 44,440	$ 4,392,943	4.0%

(1) Net weighted average coupon as of December 31, 2014 is presented net of servicing and other fees.

(2)

Agency RMBS IOs and IIOs, Non-Agency RMBS IOs and IIOs, Agency and Non-Agency IOs and IIOs, accounted for as derivatives, and Agency and Non-Agency CMBS IOs and IIOs have no principal balances and bear interest based on a notional balance. The notional balance is used solely to determine interest distributions on interest-only class of securities. At December 31, 2014, the notional balance for Agency RMBS IOs and IIOs, Non-Agency IOs and IIOs, Agency, Non-Agency IOs and IIOs, accounted for as derivatives, and CMBS IOs and IIOs was $1.2 billion, $329.7 million, $818.7 million and $46.6 million, respectively.

(3) Interest on these securities is reported as a component of Gain (loss) on derivative instruments, net.

(4) Other securities includes a residual interest in asset-backed securities which has no principal balance and an amortized cost of approximately $7.4 million.

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The following table summarizes our MBS and other securities at fair value according to their estimated weighted average life classifications as of December 31, 2014 (dollars in thousands):

Weighted Average Life	Fair Value, Including Linked Transactions (Non-GAAP)	Fair Value, Linked Transactions	Fair Value (GAAP Basis)	Net Weighted Average Coupon (GAAP Basis)(1)	Net Weighted Average Coupon (Non-GAAP Basis)(1)
Less than or equal to three years	$ 80,639	$ 6,002	$ 74,637	5.5%	5.6%
Greater than three years and less than or equal to five years	955,319		955,319	4.0%	4.0%
Greater than five years and less than or equal to 10 years	3,089,052	32,608	3,056,444	3.7%	3.8%
Greater than 10 years	313,197	13,874	299,323	5.3%	5.5%
Total	$ 4,438,207	$ 52,484	$ 4,385,723	4.0%	4.0%

(1) Net weighted average coupon as of December 31, 2014 is presented net of servicing and other fees.

The following tables summarize certain characteristics of our Agency RMBS portfolio by issuer and investment category as of December 31, 2014 (dollars in thousands):

	Principal Balance	Amortized Cost	Fair Value	Net Weighted Average Coupon(1)
Agency RMBS 20-Year and 30-Year				
Fannie Mae	$ 1,921,555	$ 2,058,853	$ 2,069,146	4.0%
Freddie Mac	790,949	838,143	841,104	3.7
Total Agency RMBS 20-Year and 30-Year	2,712,504	2,896,996	2,910,250	3.9
Agency RMBS IOs and IIOs(2)				
Fannie Mae	N/A	53,019	59,480	3.7
Freddie Mac	N/A	38,054	39,699	3.3
Ginnie Mae	N/A	87,089	89,327	4.6
Total AgencyR MBS IOs and IIOs(2)	N/A	178,162	188,506	4.0
Agency RMBS IOs and IIOs accounted for as derivatives(2)				
Fannie Mae	N/A	N/A	22,304	3.2
Freddie Mac	N/A	N/A	11,441	4.6
Ginnie Mae	N/A	N/A	35,326	4.2
Total Agency RMBS IOs and IIOs accounted for as derivatives(2)	N/A	N/A	69,071	3.9
Total: Agency RMBS	$ 2,712,504	$ 3,075,158	$ 3,167,827	3.9%

(1) Net weighted average coupon as of December 31, 2014 is presented net of servicing and other fees.

(2) Agency RMBS IOs and IIOs, Agency RMBS IOs and IIOs, accounted for as derivatives have no principal balances and bear interest based on a notional balance. The notional balance is used solely to determine interest distributions on interest-only class of securities.

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The following table details the constant prepayment rates for our Agency portfolio as of December 31, 2014, based on our Manager's estimates which are based on third party models, as adjusted by our Manager, and are updated quarterly on a prospective basis:

Constant Prepayment Rates	Low	High
Agency RMBS		
20-Year Mortgage	2.85%	26.28%
30-Year Mortgage	5.27%	32.07%
Agency RMBS IOs and IIOs	6.36%	29.69%
Agency RMBS IOs and IIOs accounted for as derivatives	5.17%	26.73%
Agency CMBS and Agency CMBS IOs and IIOs(1)	N/A	N/A
Agency CMBS IOs accounted for as derivatives(1)	N/A	N/A

(1) CMBS generally include prepayment restrictions; therefore, there are no Constant Prepayment Rates available.

The following table presents the fair value and weighted average purchase price for each of our Non-agency RMBS categories (GAAP Basis), together with certain of their respective underlying loan collateral attributes and current performance metrics as of December 31, 2014 (fair value dollars in thousands):

Category	Fair Value	Weighted Average Purchase Price	Weighted Average Life (Years)	Original LTV	Original FICO	60+ Day Delinquent	6-Month CPR
Prime(1)	$ 96,833	$ 94.01	10.7	69.7%	727	9.8%	14.1%
Alt-A	460,687	79.51	10.1	74.0%	704	11.7%	10.1%
Subprime	121,664	68.46	11.3	78.6%	630	12.9%	8.0%
Total	$ 679,184	$ 79.60	10.4	74.2%	694	11.6%	10.3%

(1) Includes Non-Agency RMBS underlying linked transactions with a fair value of $8.2 million.

The following table summarizes the credit ratings of our Non-agency RMBS and Non-agency CMBS based on fair value as of December 31, 2014:

Non-Agency RMBS Credit Rating(1)	Percentage(2)	Non-Agency CMBS Credit Rating(1)	Percentage(3)	Other Securities Credit Rating(1)	Percentage(4)
BBB	0.1%	BBB	%	BBB	%
BBB	%	BBB	2.6%	BBB	%
BB	%	BB	2.2%	BB	13.8%
B+	%	B+	2.1%	B+	%
B	0.8%	B	4.3%	B	%
B	0.9%	B	13.6%	B	%
Below B	92.3%	Below B	50.7%	Below B	17.9%
Not Rated	5.9%	Not Rated	24.5%	Not Rated	68.3%
Total	100.0%	Total	100.0%	Total	100.0%

(1) For securities for which one or two ratings are obtained, the lowest rating is used. For securities for which three ratings are obtained, the middle rating is used. Ratings are obtained either from S&P or other rating agencies, stated in terms of the S&P equivalent.

(2) Includes the fair value of Non-Agency RMBS underlying linked transactions of $8.2 million.

(3) Includes the fair value of Non-Agency CMBS underlying linked transactions of $38.6 million.

(4) Includes the fair value of Other securities underlying linked transactions of $5.7 million.

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The following table details information for our Non-Agency and other securities portfolio as of December 31, 2014, based on our Manager's estimates which are based on third party models, as adjusted by our Manager, and are updated quarterly on a prospective basis:

	Cumulative Default		Cumulative Severity		Cumulative 5-Year CRR	
	Low	High	Low	High	Low	High
Non-Agency RMBS	6.39%	56.11%	4.00%	87.65%	6.85%	7.23%
Non-Agency RMBS IOs and IIOs	20.68%	40.23%	15.81%	78.45%	6.99%	6.99%
Non-Agency RMBS IOS and IIOs accounted for as derivatives	12.81%	22.76%	4.00%	63.52%	7.97%	7.97%
Non-Agency CMBS	%	0.50%	N/A	N/A	N/A	N/A
Other securities	%	23.89%	%	95.07%	1.00%	10.00%
Linked transactions, net, at fair value	%	28.95%	58.93%	95.07%	4.00%	8.24%

We made investments in certain Non-Agency RMBS inverse floaters. The coupon rates on these securities have an inverse relationship to a benchmark rate. When the benchmark interest rate increases the coupon payment rate will decrease because the benchmark interest rate is deducted from the coupon payment. We generally purchased these securities at a premium. Accelerated prepayments on these bonds could result in an economic loss, as we would not recover the upfront premium. The premiums are amortized into income using the effective interest rate method. As of December 31, 2014 and December 31, 2013, we held $93.9 million and $22.7 million, respectively, in Non-Agency RMBS inverse floaters excluding linked transactions. In addition as of December 31, 2014 and December 31, 2013, we held $8.2 million and $71.0 million, respectively in Non-Agency RMBS inverse floaters accounted for as linked transactions.

The following table presents certain information about our residential whole-loans investment portfolio at December 31, 2014:

Current Coupon Rate	Number of Loans	Principal Balance	Weighted Average Loan to Value	Weighted Average FICO Score	Weighted Average Life to Maturity (years)	Weighted Average Coupon Rate
4.01 - 5.00%	5	$ 3,387	63.8%	744	4.2	4.8%
5.01 - 6.00%	3	1,001	74.0%	742	3.0	5.8%
6.01 - 7.00%	7	2,044	70.6%	713	4.1	6.6%
7.01 - 8.00%	3	381	66.6%	669	4.4	7.3%
8.01 - 9.00%	1	221	75.0%	665	2.1	8.5%
Total	19	$ 7,034	67.7%	728	3.9	5.7%

The following table presents the U.S. states represented in residential whole-loans at December 31, 2014 based on principal balance:

	State Concentration	Principal Balance
California	58.1%	$ 4,085
Florida	23.8	1,675
West Virginia	9.2	649
New Jersey	4.7	327
Virginia	2.1	149
Pennsylvania	2.1	149
Total	100.0%	$ 7,034

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Investment Activity

Agency and Non-Agency RMBS, Agency and Non-Agency CMBS, IO and IIO Securities, Other Securities and Residential Whole-Loans.

The following tables present our investment portfolio activity, including linked transactions (Non-GAAP) for the years ended December 31, 2014, December 31, 2013 and for the period from May 15, 2012 (commencement of operations) through December 31, 2012 (dollars in thousands):

	For the year ended December 31, 2014		
	Purchases	Principal Payments and Basis Recovery	Proceeds from Sales
Agency RMBS and Agency RMBS IOs and IIOs	$ 2,461,316	$ 263,947	$ 1,608,541
Non-Agency RMBS	718,519	63,225	414,130
Agency CMBS and Agency CMBS IOs and IIOs	30,009	2,781	3,673
Non-Agency CMBS	549,376	1,272	168,535
Other securities	254,022	1,060	180,385
Total MBS and other securities: Excluding Linked Transactions and Residential whole-loans (GAAP)	$ 4,013,242	$ 332,285	$ 2,375,264
Residential whole-loans(1)	7,161	9	
Non-Agency RMBS Linked Transactions		4,801	6,215
Non-Agency CMBS Linked Transactions	41,656		
Other securities Linked Transactions	13,083		
Total MBS and other securities: Including Linked Transactions and Residential whole-loans (Non-GAAP)	$ 4,075,142	$ 337,095	$ 2,381,479

(1) Purchases of residential whole-loans include premiums of $131 thousand paid at acquisition.

	For the year ended December 31, 2013		
	Purchases	Principal Payments and Basis Recovery	Proceeds from Sales
Agency RMBS and Agency RMBS IOs and IIOs	$ 1,581,736	$ 288,257	$ 3,491,805
Non-Agency RMBS	349,609	17,132	108,086
Agency CMBS and Agency CMBS IOs and IIOs	20,559	385	
Non-Agency CMBS	8,325		
Other securities	44,367		20,597
Total MBS: Excluding Linked Transactions (GAAP)	$ 2,004,596	$ 305,774	$ 3,620,488
Agency RMBS Linked Transactions	9,705	58	
Non-Agency RMBS Linked Transactions	166,923	1,950	21,735
Total MBS: Including Linked Transactions (Non-GAAP)	$ 2,181,224	$ 307,782	$ 3,642,223

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	For the period from May 15, 2012 (commencement of operations) through December 31, 2012		
	Purchases	Principal Payments and Basis Recovery	Proceeds from Sales
Agency RMBS and Agency RMBS IOs and IIOs	$ 7,679,165	$ 105,681	$ 2,389,472
Non-Agency RMBS	19,147	67	
Other Securities	100,655		100,854
Total MBS (GAAP)	$ 7,798,967	$ 105,748	$ 2,490,326

For the years ended December 31, 2014 and December 31, 2013, we settled certain derivatives realizing a net gain of $1.1 million and a net gain of approximately $1.7 million, respectively from the unlinking of securities previously accounted for as derivatives through linked transactions. We reclassify, from mark-to-market, adjustments on linked transactions to realized gain (loss) on linked transactions during the period the security becomes unlinked. For the period from May 15, 2012 (commencement of operations) through December 31, 2012 we did not realize any gains or losses on unlinking of securities previously accounted for as derivatives through linked transactions.

The following table presents the vintage of our investment portfolio, including linked transactions, at December 31, 2014:

	2001	2003	2004	2005	2006	2007	2009	2010	2011	2012	2013	2014	Total
Agency RMBS													
20-Year Mortgage										5.9%	14.3%	5.2%	25.4%
30-Year Mortgage							0.3%	1.4%	0.1%	14.0%	11.6%	13.1%	40.5%
Agency Interest Only- Strips					0.2%			0.4%	0.4%	2.1%	0.7%	0.4%	4.2%
Agency and Non-Agency Interest-Only Strips, accounted for as derivatives				0.1%	0.1%			0.2%	0.1%	0.8%	0.5%		1.8%
Non-Agency RMBS		0.1%	0.5%	4.3%	4.8%	4.4%						0.9%	15.0%
Non-Agency Linked Transactions, including Non U.S.						0.2%						0.9%	1.1%
Agency and Non-Agency CMBS			0.2%		3.0%	3.3%			0.6%	0.1%		2.1%	9.3%
Other securities	0.6%		0.2%								0.7%	0.9%	2.4%
Other securities linked												0.1%	0.1%
Residential whole-loans												0.2%	0.2%
Total MBS (Non-GAAP)	0.6%	0.1%	0.9%	4.4%	8.1%	7.9%	0.3%	2.0%	1.2%	22.9%	27.8%	23.8%	100%

As of December 31, 2014 the weighted average expected remaining term to the expected maturity of our investment portfolio, including linked transactions is 6.7 years.

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Financing and Other Liabilities. We have entered into repurchase agreements to finance a substantial majority of our MBS and other securities. These agreements are secured by substantially all of our MBS and other securities and bear interest at rates that have historically moved in close relationship to LIBOR. The following table summarizes the fair value of MBS and other collateral pledged as of December 31, 2014, December 31, 2013 and December 31, 2012.

	December 31, 2014		December 31, 2013		December 31, 2012	
Collateral	**Repurchase Agreement Borrowings Outstanding**	**Fair Value of Collateral Pledged(1)**	**Repurchase Agreement Borrowings Outstanding**	**Fair Value of MBS Collateral Pledged**	**Repurchase Agreement Borrowings Outstanding**	**Fair Value of MBS Collateral Pledged**
Agency RMBS	$ 2,994,351	$ 3,158,544	$ 2,331,276	$ 2,463,347	$ 4,794,730	$ 5,043,824
Non-Agency RMBS	473,942	670,526	208,923	305,318		
Agency and Non-Agency CMBS	325,864	431,938	17,544	23,597		
Other securities(1)	81,564	108,743	21,324	26,685		
Total: Excluding Linked Transactions	$ 3,875,721	$ 4,369,751	$ 2,579,067	$ 2,818,947	$ 4,794,730	$ 5,043,824
Non-Agency RMBS Linked Transactions	6,559	8,156	61,187	79,746		
Non-Agency CMBS Linked Transactions, including Non U.S.	22,458	38,609				
Other securities Linked Transactions	2,840	5,719				
Total: Including Linked Transactions (Non-GAAP)	$ 3,907,578	$ 4,422,235	$ 2,640,254	$ 2,898,693	$ 4,794,730	$ 5,043,824

(1) Other securities includes repurchase borrowings of $4.9 million and collateral pledged attributed to residential whole-loans owned through trust certificates with a fair value of $7.2 million at December 31, 2014. The trust certificates are eliminated upon consolidation.

The following table presents our borrowing activity, by type of collateral pledged, for the years ended December 31, 2014 and December 31, 2013 and for the period from May 15, 2012 (commencement of operations) through December 31, 2012:

	For the year ended December 31, 2014		For the year ended December 31, 2013		For the period from May 15, 2012 (commencement of operations) through December 31, 2012	
Collateral	**Proceeds**	**Repayments**	**Proceeds**	**Repayments**	**Proceeds**	**Repayments**
Agency RMBS	$ 17,888,989	$ 17,225,914	$ 28,892,822	$ 31,356,276	$ 14,511,707	$ 9,716,977
Non-Agency RMBS	2,889,924	2,624,905	942,758	733,835		
Agency and Non-Agency CMBS	1,425,232	1,116,912	35,963	18,419		
Other securities(1)	615,841	555,601	76,663	55,339		
Total: Excluding Linked Transactions	$ 22,819,986	$ 21,523,332	$ 29,948,206	$ 32,163,869	$ 14,511,707	$ 9,716,977
Agency RMBS Linked Transactions			18,618	18,618		
Non-Agency RMBS Linked Transactions	126,769	181,396	146,471	85,284		
Non-Agency CMBS Linked Transactions, including Non U.S.	44,785	20,240				
Other securities Linked Transactions	9,381	6,541				
Total	$ 23,000,921	$ 21,731,509	$ 30,113,295	$ 32,267,771	$ 14,511,707	$ 9,716,977

(1) Other securities includes repurchase borrowings proceeds of $4.9 million and repayments of $0 for borrowings collateralized by residential whole-loans owned through trust certificates for the year ended December 31, 2014. The trust certificates are eliminated upon consolidation.

As discussed further in Note 2 Revision of Previously Issued Financial Statements for Errors Affecting Certain Items Presented in the Statements of Cash Flows and Notes to Financial Statements, we have elected to revise our presentation of borrowing activity, by type of collateral pledged, for the three and six months ended June 30, 2014 and for the nine months ended September 30, 2014 when they are next filed in our quarterly financial statements on Form 10-Q for the quarters ending June 30, 2015 and September 30, 2015 to correct these errors.

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The effect of these errors on the tables presenting our borrowing activity, by type of collateral pledged, for the three and six months ended June 30, 2014 and the nine months ended September 30, 2014 (summarized):

As Originally Reported

(dollars in thousands)	For the three months ended June 30, 2014		For the six months ended June 30, 2014	
Collateral	Proceeds	Repayments	Proceeds	Repayments
Non-Agency RMBS	$ 896,241	$ 649,327	$ 1,321,850	$ 1,026,040
All other items with no changes	6,573,384	5,532,011	10,478,368	9,241,997
Total: Excluding Linked Transactions	$ 7,469,625	$ 6,181,338	$ 11,800,218	$ 10,268,037
All other Linked Transactions items with no changes	52,436	37,670	91,007	124,714
Total	$ 7,522,061	$ 6,219,008	$ 11,891,225	$ 10,392,751

Adjustments

(dollars in thousands)	For the three months ended June 30, 2014		For the six months ended June 30, 2014	
Collateral	Proceeds	Repayments	Proceeds	Repayments
Non-Agency RMBS	$ (2,757)	$ (2,757)	$ (2,757)	$ (2,757)
All other items with no changes				
Total: Excluding Linked Transactions	$ (2,757)	$ (2,757)	$ (2,757)	$ (2,757)
All other Linked Transactions items with no changes				
Total	$ (2,757)	$ (2,757)	$ (2,757)	$ (2,757)

Revised

(dollars in thousands)	For the three months ended June 30, 2014		For the six months ended June 30, 2014	
Collateral	Proceeds	Repayments	Proceeds	Repayments
Non-Agency RMBS	$ 893,484	$ 646,570	$ 1,319,093	$ 1,023,283
All other items with no changes	6,573,384	5,532,011	10,478,368	9,241,997
Total: Excluding Linked Transactions	$ 7,466,868	$ 6,178,581	$ 11,797,461	$ 10,265,280
All other Linked Transactions items with no changes	52,436	37,670	91,007	124,714
Total	$ 7,519,304	$ 6,216,251	$ 11,888,468	$ 10,389,994

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As Originally Reported

(dollars in thousands) Collateral	For the nine months ended September 30, 2014 Proceeds	Repayments
Non-Agency RMBS	$ 2,203,422	$ 1,943,680
All other items with no changes	15,960,768	14,917,450
Total: Excluding Linked Transactions	$ 18,164,190	$ 16,861,130
All other Linked Transactions items with no changes	142,530	178,948
Total	$ 18,306,720	$ 17,040,078

Adjustments

(dollars in thousands) Collateral	For the nine months ended September 30, 2014 Proceeds	Repayments
Non-Agency RMBS	$ (2,757)	$ (2,757)
All other items with no changes		
Total: Excluding Linked Transactions	$ (2,757)	$ (2,757)
All other Linked Transactions items with no changes		
Total	$ (2,757)	$ (2,757)

Revised

(dollars in thousands) Collateral	For the nine months ended September 30, 2014 Proceeds	Repayments
Non-Agency RMBS	$ 2,200,665	$ 1,940,923
All other items with no changes	15,960,768	14,917,450
Total: Excluding Linked Transactions	$ 18,161,433	$ 16,858,373
All other Linked Transactions items with no changes	142,530	178,948
Total	$ 18,303,963	$ 17,037,321

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At December 31, 2014, we had outstanding repurchase agreement borrowings with the following 21 counterparties totaling approximately $3.9 billion, which is a Non-GAAP measure due to our Linked Transactions, which is reconciled to GAAP below as follows:

(dollars in thousands) Repurchase Agreement Counterparties	Amount Outstanding	Percent of Total Amount Outstanding	Fair Value of Company Securities Held as Collateral(2)	Counterparty Rating(3)
Merrill Lynch Pierce Fenner & Smith Inc.(1)	$ 598,717	15.3%	$ 621,152	A
Deutsche Bank Securities LLC(1)	442,131	11.3%	482,107	A
Barclays Capital Inc.(1)	364,609	9.3%	413,245	A
JP Morgan Securities LLC(1)	353,676	9.1%	382,364	A+
BNP Paribas Securities Corporation(1)	336,531	8.6%	359,216	A+
Royal Bank of Canada(1)	275,065	7.0%	371,280	AA
UBS Securities LLC(1)	256,405	6.6%	307,947	A
Credit Suisse Securities (USA) LLC(1)	241,541	6.2%	326,785	A
Goldman Sachs Bank USA(1)	236,873	6.1%	246,796	A
Mizuho Securities USA Inc.(1)	204,755	5.2%	231,506	(P)A2
Morgan Stanley & Co. LLC(1)	157,926	4.0%	162,348	A
Jefferies & Company Inc.(1)	77,098	2.0%	81,930	BBB
RBC Capital Markets LLC(1)	75,003	1.9%	78,413	AA
RBC (Barbados) Trading Bank Corporation(1)	54,561	1.4%	73,266	P-1
The Royal Bank of Scotland plc(1)	51,252	1.3%	70,333	A
Wells Fargo Bank NA(1)	50,984	1.3%	53,635	AA
Nomura Securities International, Inc.(1)	41,226	1.1%	42,449	Unrated(4)
Citigroup Global Markets Inc.(1)	32,100	0.8%	42,399	A
Deutsche Bank AG(1)	27,362	0.7%	41,866	A
KGS-Alpha Capital Markets, L.P.	23,789	0.6%	25,229	Unrated
Wells Fargo Securities LLC	5,974	0.2%	7,968	AA
Total: Non-GAAP Basis Including Linked Transactions, including Non U.S.	$ 3,907,578	100.0%	$ 4,422,234	
Linked Transactions	31,857		52,483	
Total: GAAP Basis Excluding Linked Transactions	$ 3,875,721		$ 4,369,751	

(1) Counterparty holds collateral valued in excess of 5% of our stockholders' equity as security for our obligations under the applicable repurchase agreements as of December 31, 2014.

(2) Fair value of Company securities held as collateral includes residential whole-loans owned through trust certificates with a fair value of $7.2 million.

(3) The counterparty ratings presented above are the long-term issuer credit ratings as rated at December 31, 2014 by S&P, except for Mizuho Securities USA Inc. which is the long-term issuer credit rating by Moody's at December 31, 2014 and for RBC (Barbados) Trading Bank Corporation which is the short-term issuer credit rating by Moody's at December 31, 2014.

(4) Nomura Holdings, Inc., the parent company of Nomura Securities International, Inc., is rated BBB+ by S&P at December 31, 2014.

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At December 31, 2013, we had outstanding repurchase agreement borrowings with the following 16 counterparties totaling approximately $2.6 billion, which is a Non-GAAP measure due to our Linked Transactions, which is reconciled to GAAP below as follows:

(dollars in thousands) Repurchase Agreement Counterparties	Amount Outstanding	Percent of Total Amount Outstanding	Fair Value of Company MBS Held as Collateral	Counterparty Rating(2)
Barclays Capital Inc.(1)	$ 362,476	13.7%	$ 414,344	A
Deutsche Bank Securities LLC(1)	356,372	13.5%	381,319	A
Goldman Sachs Bank USA(1)	306,708	11.6%	328,504	A
JP Morgan Securities LLC(1)	271,887	10.3%	313,967	A+
Citigroup Global Markets Inc.(1)	205,856	7.8%	213,358	A
Credit Suisse Securities (USA) LLC(1)	178,896	6.8%	235,680	A
Mizuho Securities USA Inc.(1)	173,030	6.6%	178,101	(P)A2
BNP Paribas Securities Corporation.(1)	152,084	5.8%	164,025	A+
Merrill Lynch Pierce Fenner & Smith Inc.(1)	142,665	5.4%	148,351	A
UBS Securities LLC(1)	130,833	5.0%	133,938	A
South Street Securities LLC(1)	100,818	3.8%	105,020	AA+
Jefferies & Company Inc.(1)	100,762	3.8%	104,302	BBB
RBC Capital Markets LLC(1)	56,222	2.1%	61,898	AA
RBS Securities Inc.(1)	51,138	1.9%	52,625	A
The Royal Bank of Scotland plc(1)	37,993	1.4%	50,834	BBB+
Morgan Stanley & Co. LLC	12,514	0.5%	12,427	A
Total: Non-GAAP Basis Including Linked Transactions	$ 2,640,254	100.0%	$ 2,898,693	
Linked Transactions	61,187		79,746	
Total: GAAP Basis Excluding Linked Transactions	$ 2,579,067		$ 2,818,947	

(1) Counterparty holds collateral valued in excess of 5% of our stockholders' equity as security for our obligations under the applicable repurchase agreements as of December 31, 2013.

(2) The counterparty ratings presented above are the long-term issuer credit ratings as rated at March 12, 2014 by S&P, except for Mizuho Securities USA Inc. which is the long-term issuer credit rating by Moody's at March 12, 2014.

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At December 31, 2012, we had outstanding repurchase agreement borrowings with the following 14 counterparties totaling approximately $4.8 billion:

(dollars in thousands) Repurchase Agreement Counterparties	Amount Outstanding	Percent of Total Amount Outstanding	Fair Value of Company MBS Held as Collateral
Deutsche Bank Securities LLC	$ 730,227	15.2%	$ 763,876
JP Morgan Securities LLC	575,880	12.0%	619,547
Citigroup Global Markets Inc.	481,252	10.0%	504,712
Barclays Capital Inc.	398,172	8.3%	419,038
BNP Paribas Securities Corporation	361,701	7.5%	382,338
Mizuho Securities USA Inc.	308,740	6.4%	323,329
Credit Suisse Securities (USA) LLC	300,222	6.3%	311,860
RBC Capital Markets LLC	292,648	6.1%	307,461
Merrill Lynch Pierce Fenner & Smith Inc.	262,082	5.5%	273,770
Morgan Stanley & Co. LLC	253,862	5.3%	264,412
Goldman Sachs Bank USA	247,416	5.2%	261,553
Wells Fargo Securities LLC & Wells Fargo Bank N.A.	199,087	4.2%	209,171
UBS Securities LLC	197,947	4.1%	207,233
Jefferies & Company Inc.	185,494	3.9%	195,524
Total	$ 4,794,730	100.0%	$ 5,043,824

We record the liability for MBS and other securities purchased, for which settlement has not taken place as an investment related payable. As of December 31, 2014, we had investment related payables of $166.6 million of which no items were outstanding greater than 30 days.

The following table presents our borrowings by type of collateral pledged as of December 31, 2014, December 31, 2013 and December 31, 2012, and the respective Cost of Funds for the periods then ended (dollars in thousands):

Collateral	Balance (GAAP) December 31, 2014	Weighted Average Cost of Funds for the year ended December 31, 2014	Balance (GAAP) December 31, 2013	Weighted Average Cost of Funds for the year ended December 31, 2013	Balance (GAAP) December 31, 2012	Weighted Average Cost of Funds for the period from May 15, 2012 (commencement of operations) through December 31, 2012
Agency RMBS	$ 2,994,351	0.38%	$ 2,331,276	0.43%	$ 4,794,730	0.45%
Non-Agency RMBS	473,942	1.62	208,923	1.76		
Agency and Non-Agency CMBS	325,864	1.51	17,544	1.39		
Other securities(1)	81,564	1.48	21,324	2.00		
Total	$ 3,875,721	0.60%	$ 2,579,067	0.47%	$ 4,794,730	0.45%

(1) Other securities include repurchase borrowings of $4.9 million collateralized by residential whole-loans owned through trust certificates at December 31, 2014. The trust certificates are eliminated upon consolidation.

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The following table presents our borrowings by type of collateral pledged as of December 31, 2014, December 31, 2013 and December 31, 2012, and the respective Effective Cost of Funds (Non-GAAP financial measure) for the periods then ended (dollars in thousands) See "Non-GAAP financial measures":

Collateral	Balance (Non-GAAP) December 31, 2014	Weighted Average Effective Cost of Funds for the year ended December 31, 2014(1)	Balance (Non-GAAP) December 31, 2013	Weighted Average Effective Cost of Funds for the year ended December 31, 2013(1)	Balance (Non-GAAP) December 31, 2012	Weighted Average Effective Cost of Funds for the period from May 15, 2012 (commencement of operations) through December 31, 2012(1)
Agency RMBS	$ 2,994,351	1.31%	$ 2,331,276	1.05%	$ 4,794,730	0.80%
Non-Agency RMBS	473,942	1.83	208,923	1.76		
Agency and Non-Agency CMBS	325,864	2.08	17,544	1.39		
Other securities(2)	81,564	1.48	21,324	2.00		
Total: Excluding Linked Transactions	$ 3,875,721	1.41%	$ 2,579,067	1.08%	$ 4,794,730	0.80%
Agency RMBS Linked Transactions				0.38		
Non-Agency RMBS Linked Transactions	6,559	1.65	61,187	1.78		
Non-Agency CMBS Linked Transactions, including Non U.S.	22,458	1.94				
Other Securities Linked Transactions	2,840	2.00				
Total	$ 3,907,578	1.41%	$ 2,640,254	1.08%	$ 4,794,730	0.80%

(1) The effective cost of funds for the years ended December 31, 2014 and December 31, 2013 and for the period from May 15, 2012 (commencement of operations) through December 31, 2012, are calculated on an annualized basis and include interest expense for the periods and net periodic interest payments on interest rate swaps, net of premium amortization on MAC swaps, of approximately $29.9 million, $22.9 million and $6.3 million, respectively, interest payments on Agency RMBS linked transactions of approximately $0, $6 thousand and $0, respectively, interest payments on Non-Agency RMBS linked transactions of approximately $346 thousand, $265 thousand and $0, respectively, interest payments on Non-Agency CMBS linked transactions of approximately $167 thousand, $0 and $0, respectively, and interest payments on other securities linked transactions of approximately $33 thousand, $0 and $0, respectively. While swaps are not accounted for using hedge accounting, such instruments are viewed by us as an economic hedge against increases in interest rates on our liabilities and are classified as hedges for purposes of satisfying the REIT requirements. In addition, although certain securities and their respective repurchase borrowings are classified as derivatives, we view the interest expense attributed to these borrowings as additional cost of funds. See "Non-GAAP Financial Measures."

(2) Other securities include repurchase borrowings of $4.9 million for residential whole-loans owned through trust certificates at December 31, 2014. The trust certificates are eliminated upon consolidation.

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The following table presents our average borrowings, by type of collateral pledged, on a GAAP and Non-GAAP basis for the years ended December 31, 2014 and December 31, 2013, and for the period from May 15, 2012 (commencement of operations) through December 31, 2012 (in thousands):

Collateral	For the year ended December 31, 2014	For the year ended December 31, 2013	For the period from May 15, 2012 (commencement of operations) through December 31, 2012
Agency RMBS	$ 3,019,411	$ 3,681,656	$ 2,840,999
Non-Agency RMBS	393,426	114,053	
Agency and Non-Agency CMBS	218,995	4,525	
Other securities(1)	67,275	5,257	
Total: Excluding Linked Transactions (GAAP)	$ 3,699,107	$ 3,805,491	$ 2,840,999
Agency RMBS Linked Transactions (Non-GAAP)		1,575	
Non-Agency RMBS Linked Transactions (Non-GAAP)	20,859	14,860	
Non-Agency CMBS Linked Transactions (Non-GAAP), including Non U.S.	8,588		
Other securities Linked Transactions (Non-GAAP)	1,652		
Total (Non-GAAP)	$ 3,730,206	$ 3,821,926	$ 2,840,999
Maximum borrowings during the period (Non-GAAP)(2)	4,258,778	4,808,778	4,900,556

(1) Other securities include average repurchase borrowings of $1.2 million for residential whole-loans owned through trust certificates for the year ended December 31, 2014. The trust certificates are eliminated upon consolidation.

(2) Amount represents the maximum borrowings at month-end during each of the respective periods.

Derivative Instruments. As of December 31, 2014, we had entered into swaps designed to mitigate the effects of increases in interest rates under a portion of our repurchase agreements as such repurchase agreements are renewed and/or extended. The swaps generally provide for fixed interest rates that are indexed off of LIBOR and are viewed by us to effectively fix the floating interest rates, on our repurchase agreements. In managing our interest rate swap position in conjunction with our hedging strategy and potential tax implications, we may enter into variable-rate payment swaps which effectively act as an offset to fixed-rate payment swaps. As of December 31, 2014, we had approximately $2.1 billion of variable-rate payment swaps in addition to $110.0 million of forward starting variable-rate payment swaps.

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The following table presents information about our fixed pay rate interest rate swaps as of December 31, 2014 and December 31, 2013 (dollars in thousands):

	December 31, 2014				
Remaining Interest Rate Swap Term	Notional Amount	Fair Value Asset (Liability), net	Average Fixed Pay Rate	Average Maturity (Years)	Forward Starting
1 year or less	$ 89,300	$ (111)	0.5%	0.9	%
Greater than 1 year and less than 3 years	1,972,300	(733)	0.8	1.8	20.3
Greater than 3 years and less than 5 years	603,000	(4,597)	1.8	4.2	
Greater than 5 years	3,103,770	(156,952)	2.8	9.4	63.1
Total	$ 5,768,370	$ (162,393)	2.0%	6.2	40.9%

	December 31, 2013				
Remaining Interest Rate Swap Term	Notional Amount	Fair Value Asset (Liability), net	Average Fixed Pay Rate	Average Maturity (Years)	Forward Starting
1 year or less	$ 215,900	$ (141)	0.4%	0.8	%
Greater than 1 year and less than 3 years	179,100	(216)	0.5	1.9	
Greater than 3 years and less than 5 years	574,200	5,630	1.3	4.4	
Greater than 5 years	1,718,650	87,857	2.4	10.8	28.6
Total	$ 2,687,850	$ 93,130	1.9%	8.0	18.3%

The following table presents information about our variable pay rate interest rate swaps as of December 31, 2014 and December 31, 2013 (dollars in thousands):

	December 31, 2014				
Remaining Interest Rate interest rate swap Term	Notional Amount	Fair Value Asset (Liability), net	Average Variable Pay Rate	Average Maturity (Years)	Forward Starting
Greater than 1 years and less than 3 years	$ 220,000	$ (164)	0.2%	2.0	%
Greater than 3 years and less than 5 years	634,000	2,210	0.2	4.5	
Greater than 5 years	1,309,600	45,229	0.2	12.1	8.4
Total	$ 2,163,600	$ 47,275	0.2%	8.8	5.1%

	December 31, 2013				
Remaining Interest Rate interest rate swap Term	Notional Amount	Fair Value Asset (Liability), net	Average Variable Pay Rate	Average Maturity (Years)	Forward Starting
Greater than 3 years and less than 5 years	$ 81,000	$ (475)	0.2%	4.8	%
Greater than 5 years	46,000	(1,243)	0.2	24.1	
Total	$ 127,000	$ (1,718)	0.2%	11.8	%

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The following tables present information about our interest rate swaptions as of December 31, 2014 and December 31, 2013 (dollars in thousands):

	December 31, 2014						
	Option			Underlying Swap			
Fixed-Pay Rate for Underlying Swap	Fair Value		Weighted Average Months Until Option Expiration	Notional Amount		Weighted Average Swap Term (Years)
2.26 - 2.50%	$	178	17.8	$	105,000	1.0
	$	178	17.8	$	105,000	1.0